FOCAL POINT |
Removing Reporting Silos In Middle Market Companies

Value Creation Pillar:
Financial and Operational Reporting Alignment

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"Professionalization of process and reporting transparency" is frequently a crucial component within the investment thesis of private equity-backed middle market acquisitions. Enhancing data structure and empowering leadership with tech-enabled tools, soundboards and reporting integrity are generally the initial value pillars supported by the playbook foundation. Developing and implementing a pragmatic cadence for regular check-in and reporting expectations is an initial challenge. Expectations for management must be clearly outlined at the outset. Reporting changes and professionalization of processes must be defined through rigorous process mapping, technology assessment, and KPI development focused on what drives the business. Ultimately, the operational KPIs must be clear & consistent, decision-supporting, trustworthy, and tied to financial results.

Simply put, prior to institutional investments entering the capital structure, many middle market companies ran their businesses more on historic assumptions, and unvalidated evidence to achieve an inherent level of growth. Decision paths were forged based on founder-owner experience and judgment with trust placed in comments like "we have done this, and we have been in the business for 20 years+". Data-driven strategies have not been part of the toolbox for most middle market businesses. To grow faster and beyond the natural trajectory laid out by the founders, firms must professionalize their decision-making through data science & visualization, astute technology integration, and providing management with a firm grasp of how their operational decisions impact the financial statements.

Starting is always the challenge. Private equity firms need to insert themselves early in the acquisition process (last stage diligence-close-first 3 months) to assess and define the core reporting needs and engage the CFO and COO suites to gain visibility of backwards-looking reports and KPIs. Forward-looking enhanced KPIs and reporting emerge as the C-suites drives the transformation in months 3-30.

I. Assessment of Data Assets

Some of the root causes of less-than-optimal reporting alignment to a firm's strategy are tied up in the following areas:

- Lack of a data culture
- Data governance + lack of transparency
- Disparate data sets + lack of a data lake
- Misunderstood data value, applications, and use of the data assets

Lack of holistic execution of past reporting & data analytics initiatives is a core problem. Fast-growing companies run the risk of not paying enough attention to their overall data hierarchy maintaining functional integrity and cascading across divisions/departments/locations/responsibilities.

This results in Operations-Finance and even Sales-Marketing to take some, but not all, of the disparate data sets and build their own dashboards. The presence of ad hoc reporting at the behest of managers is an indication of major reporting problems. Data hierarchy is not providing the cascading information the team needs to make timely decisions. Metrics development is being generated outside of enterprise-wide information systems, and there may even be a redundant, wasteful level of effort to get the ad hoc reports generated. Ad hoc reporting further perpetuates a lack of sharing among the core silos. Rather than validating data sets and coordinating information across the enterprise, executives and management are making decisions and drawing conclusions based on incomplete silos of data rather than a unified set.

Some reporting silo remedies can include:

- Begin with a charter around data governance
- Focus on data cleansing efforts and data hierarchy build-ups
- Have the stakeholder/program transformation leader from Finance
- Map out metrics flows across the entire organization - rolling up and down from single Sales & Operations transactions to the organization's financial statements
- Inventory all data sets and sources
- Define an optimal outcome (what does success look like?)
- Start with building a new data lake that will be preserved as the known trusted source
- Understand the frequency of KPI reviews, who uses the reporting to make decisions on running the business, and who is responsible for data integrity
- Provide context to the reports with baselines, historical trending, leading & lagging indicators, and SMART performance goals
- Err on the side of highly visual. Most managers and executives appreciate visual approaches to metrics rather than data tables – work with the team to make the dashboards easy to read and interpret. Teams should spend more time on action plans and decisions, not interpreting the KPIs or questioning reporting integrity
- Train the team on data flow, trending analysis, decision-making, and how their own management decisions and responsibilities impact financial results for the company as a whole

Two other questions impacting reporting hierarchies include:

1. Who will manage cyber and security strategy of this new data lake and future reports?
2. Will all this be migrated to the cloud or stored in-house?

These aspects are usually pushed for review at a time when new software and technology systems are considered. Outlining the issues and beginning discussions early ensures they do not get lost and do not proliferate more data flow and reporting workarounds over time.

II. Tech Stack Transformation

The data review is on-going as the organization adjusts to new information sources, customer behaviors, and management decision-support needs. Technology selection will play an outsized role in reducing silos and weave into the larger coordination of strategy, growth development, value creation, and ultimately, private equity returns. The business model and value creation levers will drive reporting requirements. However, private equity teams should work with portfolio management to assess current technology usage, systems & software, and current tech partner ecosystem, then, develop a roadmap to meet reporting requirements while amplifying returns from technology spend. After that review, the consideration of delete, keep, update, or add new modules and software tools can occur. The core areas to review impacting revenue and margin growth include:

- Customer Relationship Management (CRM) systems
- E-Commerce platforms
- Business Intelligence (BI) and Analytics tools
- Marketing Automation and Content Management System (CMS) software
- Operations Management systems
- Enterprise Resource Planning (ERP) systems
- Human Resources Information Systems (HRIS)
- Financial Reporting systems

III. What should a reporting transformation include for an acquired middle market company?

A | Revenue Growth — ensure all drivers of organic top line growth are captured including pipeline, close rate, time in pipeline and then slicing that by go-to-market (GTM) segment, by region, by salesperson, and alignment to goals

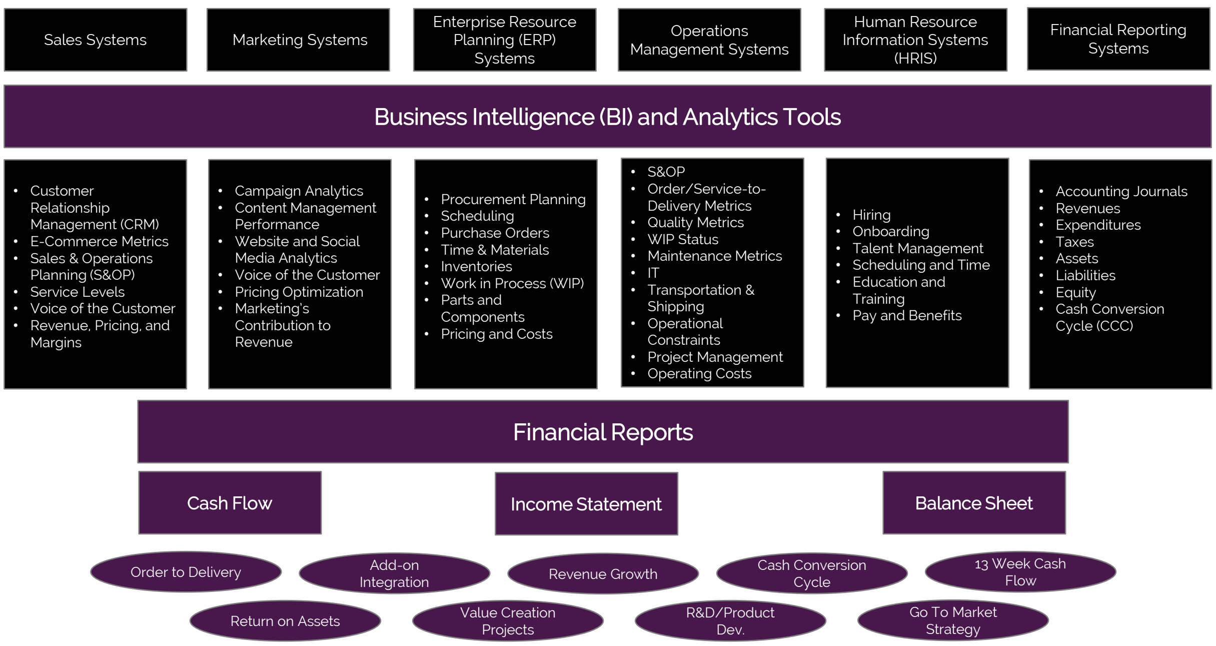
B | Finance — 13-week cash flow, cash bridge to EBITDA, cash conversion cycle (CCC), financial flash reports, and 3 core financial statements

The linkage is ensuring the order-to-cash (OTC) module is simplified and aligned.

C | Operations — order-to-delivery performance, initiative tracking, return on assets (ROA), products & services generation, operational constraints, tracking goals. The linkage to Finance is alignment to the strategic goals and value creation math tracking. Most of all, former silos need trend data for at least three years once the KPIs and BI views are re-illuminated.

D | Research & Development (R&D) — engineering progress, new products & services, voice of the customer data, and customer experience (CX) metrics

The operational linkages to Finance and alignment of value creation initiatives to strategic goals do not happen in isolation. Most organizations are too busy running the business to design data flow and reporting with integrity and scalability. Yet, doing so pays off with a deeper understanding of an organization's customers, faster EBITDA growth, more well-planned technology expenditures, alleviation of energy-draining frustrations for employees, and reduction of less-than-optimal management decision-making. All this adds up to a stronger company generating higher returns on investment.



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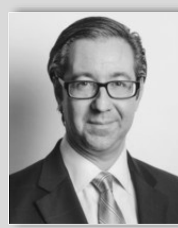
Steve leads the Private Equity Practice for Catalyft LLC, a practitioner-led, boutique operating partner firm focused on strategy implementation and operational improvements in Middle Market businesses acquired by Private Equity, investment firms and Family Offices. Steve has held several senior executive positions with the sovereign wealth fund Abu Dhabi Investment Company, Huron Consulting Group, and as C-level executive and Board member of private firms in the US, Europe and Middle East. He earned his MBA from Harvard Business School and has two Bachelor of Science degrees in Mechanical and Materials and Metallurgical Engineering from University of Michigan, Ann Arbor. Steve speaks conversational Greek, German and Arabic.



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John is a is a Transformation and Operational Excellence Leader in Private Equity Firms and Portfolio Companies. John has played many roles in the private capital space over 30 years Including senior executive to fast growing Middle Market companies, Independent Sponsor, PE and Family Office Advisor and Consulting Practice Leader. John has a BA in Economics from Fairfield University and his MBA from Pace University.