Locusts – Our Good Friends

Private equity firms are no specter to fear

When we think of grasshoppers, most people see a natural meadow in front of them, where cute grasshoppers cavort - or an insect appearing in the swarm, which attacks the fields and leaves them bare.

The latter association has probably also led to the fact that investment companies and private equity (PE) firms have been popularly called locusts for about 15 years - a name that the sector still cannot get rid of today. According to this idea, PE firms buy up companies, take them out financially, wreck them and then sell them on with huge profits, without taking the employees into consideration. There is something true about every stereotype, but the business model of PE firms has changed noticeably in recent years: from a purely financially driven focus to one of a strategic investor.

Large companies, including those in the chemical and life science industries, regularly review their strategies. They sometimes find that a product group or business unit no longer fits into their portfolio from a strategic or economic point of view. If this is the case, they look for opportunities to sell these businesses. The first choice is often a strategic buyer who sees this as a good fit for their portfolio. But PE firms are also an integral part of these sales rounds - and rightly so, because they offer a great opportunity. With the help of the new management and the new capital, the outsourced company can consistently optimize processes and realign the business model.

Of course, the PE firm wants to make a profit - but which industrial company doesn't? However, the interaction between the PE firm and the acquired business unit of the company, given the framework of portfolio management for the company, can lead to the development of a symbiotic relationship that benefits both sides.

If a company has found a company to divest, the PE firm spends a significant amount of money to buy the target, reorganize it and optimize the business model. The PE firm typically tries to do this in cooperation with company management and its employees. The company then remains in the PE firm's portfolio for a while, possibly being enlarged and strengthened through acquisitions (buy & build) before an opportunity arises for an IPO or resale - to another PE firm (secondary buy-out) or to a strategic buyer, for whom the company is now more valuable given the changes made. The acquiring organization is highly likely to find this an attractive addition to their own portfolio. In this example, the business unit that was spun off at the beginning is now integrated into a new company, while another company releases one of its business units into the cycle just described (see Fig. 1).

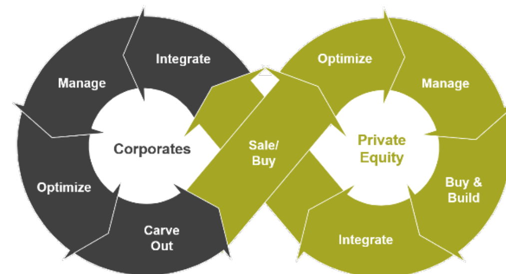

Fig. 1: Schematic representation of the symbiotic interaction between companies and PE firms for successful portfolio management within the entire industry.

What does all this have to do with a strategy consultancy like Saphenor? For strategy consultancies that focus on a specific industry sector (e.g. Saphenor for the chemical and life science industry) portfolio management projects are part of their daily business. As industry experts with outstanding process and market knowledge, their advice is worth its weight in gold and their well-founded assessment of the industry's development is of great benefit for investment decision making. Cooperation between a PE firm and a strategy consultancy can actively contribute to the success story of the new company.

PE investors make a valuable contribution to portfolio management in the chemical industry – a good reason to let the locust be just a grasshopper again.

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