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# How private investors develop their portfolio companies

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A Case study of how one of Sweden's largest private investment companies  
have developed four of its portfolio companies

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# ABSTRACT

Commercial private equity as an investment industry have quickly grown since its formation in the late 80's, and now account for a significant part of the investments made both globally and in Sweden. In 2014 the Swedish commercial private equity companies had a combined turnover of 311 billion SEK, accounting for around 9 % of Sweden's GNP.

The sector has been studied extensively by the investment industry and scholars alike due to its extraordinary growth rate. Despite this fact, very little research has been made on the private investment sector that invests in private equity. Why even fewer studies have been made in an attempt to investigate the similarities or differences between the two. Due to this research gap, this thesis' purpose is to shed some light on this relatively unstudied area, in an attempt to understand how private investors act when developing their portfolio companies through active ownership.

This is done by studying one private investment company and the development initiated by them in four of their portfolio companies. Specifically, during the five first years after having acquired the companies. This multiple case study was performed using a combination of semi-structured interviews, observations and archive analysis, with access to board material and strategical documents. Due to the confidential nature of such documents, the studied companies have been masked.

The main findings of this study is a 5-step development process, that was compiled based on the actions initiated by the investment company in its four portfolio companies. This process first focuses on the strengthening of the organization, senior management and the core activities of the company. Thereafter the focus shifts toward the more strategically important issues, as well as increasing the efficiency for the the most profitability-critical areas of the company. This is to be done gradually with a prioritization focusing not on immediate profits, but on building a stable company that will thrive in the long-run. This process needs to be flexible, where the developers needs to adapt the process for the company that is to be developed.

The development process can be used as a guideline when developing a company though require competent business developers that can identify the right actions needed for each improvement area. Not all companies have access to such competence within the company, nevertheless, it can be obtained through recruiting external members to the board of directors. Where one of the final findings of this report is the need to have the right composition in the board, which is crucial when developing a company as an active owner.

## **Key words**

Private equity, investment company, business development, private investor, development process, board of directors, development stages, Nordic, Sweden.

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I would like to take this opportunity to thank everyone who has contributed to this thesis. It has been a great opportunity for me to learn more about the investment sector and business development, areas in which I am very interested and hope to work with in many years to come.

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Ultimately, I would like to thank everyone else whom directly or indirectly have helped me with this project. This includes all of you whom have held seminars, conferences and lectures outside of the study's main scope, as well as the external interviewees whom granted me an outside in perspective of the studied company and industry.

Ultimately, I hope that this thesis will be able to grant future readers insights into the industry and some practices implemented by the private investment sector.

Thank you everyone.

Pontus Lundmark  
Lund, May 2016

# DEFINITIONS

**Family controlled private equity:**

one type of private investor that invest a family's capital in private equity. Some examples include: Axel Johnson AB and Melker Schörling AB

**Venture capital:**

Capital invested in in-mature, or start-up companies.

**Enterprise capital:**

Capital invested in mature often stable companies. (The opposite of venture capital.)

**Private equity:**

Private equity is a form of equity investment into private companies not listed on the stock exchange.

**Public equity:**

Investments made into a company listed on a stock exchange

# LIST OF ACRONYMS

<b>Avg</b>	Average
<b>CAGR</b>	Compound Annual Growth Rate
<b>DD</b>	Due Diligence
<b>EBITDA</b>	Earnings Before Interest Taxation Depreciation and Amortization
<b>HRM</b>	Human Resource Management
<b>IP</b>	Intellectual Property
<b>IPR</b>	Intellectual Property Rights
<b>KPI</b>	Key Performance Indicator
<b>M&amp;A</b>	Mergers and Acquisitions
<b>MSEK</b>	Million SEK
<b>PE</b>	Private equity
<b>PE-Fund</b>	Private equity fund
<b>RnD</b>	Research and Development



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# I BACKGROUND

This background section is aimed at granting the reader a brief introduction to the Swedish risk capital industry, with a focus on private equity. The section will present both an introduction to the industry, and its different sorts of investors. This information together with some definitions that are made in this section, will be used continuously throughout the study.

## 1.1 Introduction

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Risk capital is the capital most commonly employed when financing new ventures or business opportunities and is often seen as the oil in the machinery that is the global economy. Today, risk capital has grown to have a substantial impact on the global economy and in the companies that are invested in. Since the 80's, a relatively new investment practice have grown in importance, in both the global and Swedish economy: the private equity industry. The commercial side of private equity does today have influence over companies amounting up to around 8,8 % of Sweden's GNP according to the Swedish trade organization SVCA. This commercial segment has been studied rather extensively due to its growing importance, however, the private/family side of private equity have gone relatively un-noticed despite its large size. This thesis aims to shed some light on this private side of the private equity industry. During the first parts of this thesis, a generic framework for studying different sorts of active investors is developed. Thereafter, the framework is used to investigate one Swedish private investment company, where the goal is to grant insights into how a private investor can operate and develop its portfolio companies. (SVCA, 2016)

### 1.1.1 Investments and Risk Capital in Sweden

Different forms of risk capital have been a common sighting globally and in Sweden for many decades. In the early 1900's, the Swedish investment market was dominated by a private actors and families, whom often had close connections to the major Swedish banks. In the aftermath of the notorious *Kreuger Crash*, this somewhat changed (The Economist, 2007). Many of the largest Swedish banks had borrowed large amount of credits to the previous Kreuger empire, that became close to worthless overnight. The assets and companies that had formed the previous conglomerate were sold to a number of wealthy Swedish investors, families and spheres, which gave them a strong position as investors that would be held for many years to come (Thunholm,

1995). Not much changed except for the rising influence of the stock market up until the late 80's and early 90's (Oral source/s, 2015-2016).

Now commercial investment companies and PE-funds were introduced by some of the largest Swedish banks and insurance companies. Much based on the private equity fund structure that had been highly successful in the United States some years prior (The Economist, 2007). Some examples of such investment companies include Nordic Capital and IK investment partners that were founded in 1989, whom were soon followed by EQT and Segulah in 1994, according to their webpages (2016). Today both commercial private equity actors and the privately controlled investment companies have a large influence over the Swedish industry, due to their assorted ownership in many of Sweden's larger companies (Oral source/s, 2015-2016). Since the late 80's, the growth of the commercial private equity industry has been substantial globally, not only in Sweden. Which is clearly shown in the following diagram retrieved from Bain & Company's annual report on global private equity. Here the total number of, and the value of global buyout-backed exits are presented, clearly showing the rapid growth of the private equity sector until the financial crisis of 2008. This development has been hastened further by the current abundance on capital, caused by the low global interest rates, recovering financial markets, and an increased faith in private equity (Bain and Company, 2016).

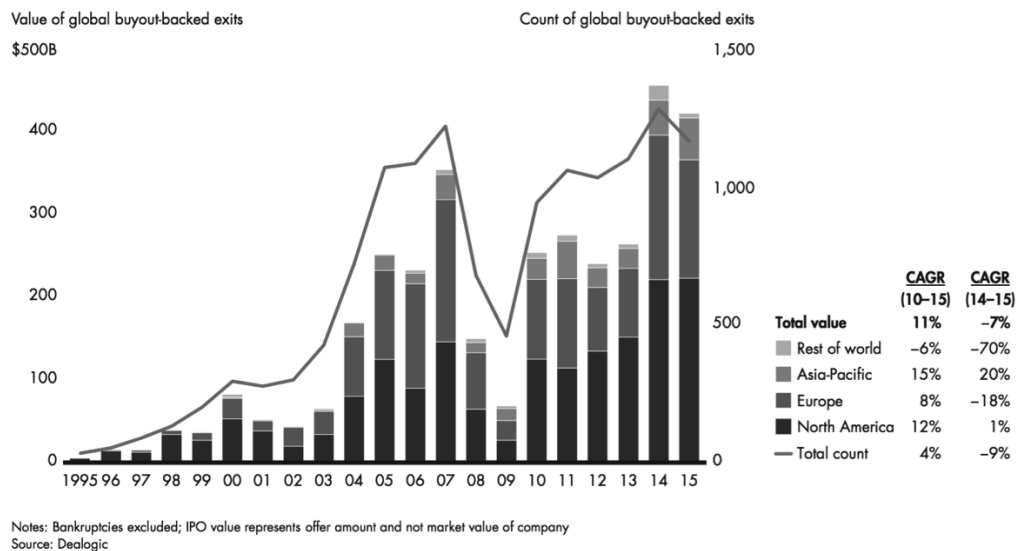


Figure 1: Value of global buy-out exits since 1995 (Bain and Company, 2016)

Today the commercial private equity companies' influence over the Swedish economy is significant. According to the Swedish trade organization SVCA, (an organization supporting risk capital investments in Sweden) commercial private equity companies owned more than 800 portfolio companies in 2014. These companies combined employ more than 200 000 people only in Sweden and have a combined turnover of 311 billion SEK, accounting for around 8,8 % of Sweden's GNP. These figures only cover their own member companies, and therefore exclude other investment companies, such as the private and family controlled ones. Companies that have a substantial influence over the Swedish economy. Regardless, the numbers give a clear indication of the private equity sector's growing influence over the Swedish industry (SVCA, 2016).

### 1.1.2 The Invested Capital's Origin

Since these companies have become such a large part of the Swedish industry, it is important to understand where the capital comes from, thereby understanding the motives of these investment companies.

The private and family controlled investment companies are generally financed through their own wealth and equity, often built through successful entrepreneurship or historical investments. This often transparent structure grants an understanding of the company's ownership, which according to many private investors lead to an increasing sense of accountability (Oral source/s, 2015-2016).

The commercial actors' ownership structure is much more complex, with disperse and often obscure ownership. In general, external investors invest in a fund or similar product, that is managed by a third party, often a so called private equity fund. The origin of the capital behind SVCA's members within commercial private equity can be found in the following diagrams, where most of SVCA's larger members are private equity funds. Where the diagram show that there is a significant difference in ownership between the commercial and privately controlled investment companies. The origin of the investors show that the Swedish private equity industry is now relatively international, where foreign investors now invest in both public private companies (Riksrevisionen, 2014). Furthermore, SVCA further points out there is a trend of increasing international ownership, conversely seen by Swedish investors whom are increasing their foreign investments (SVCA, 2016).

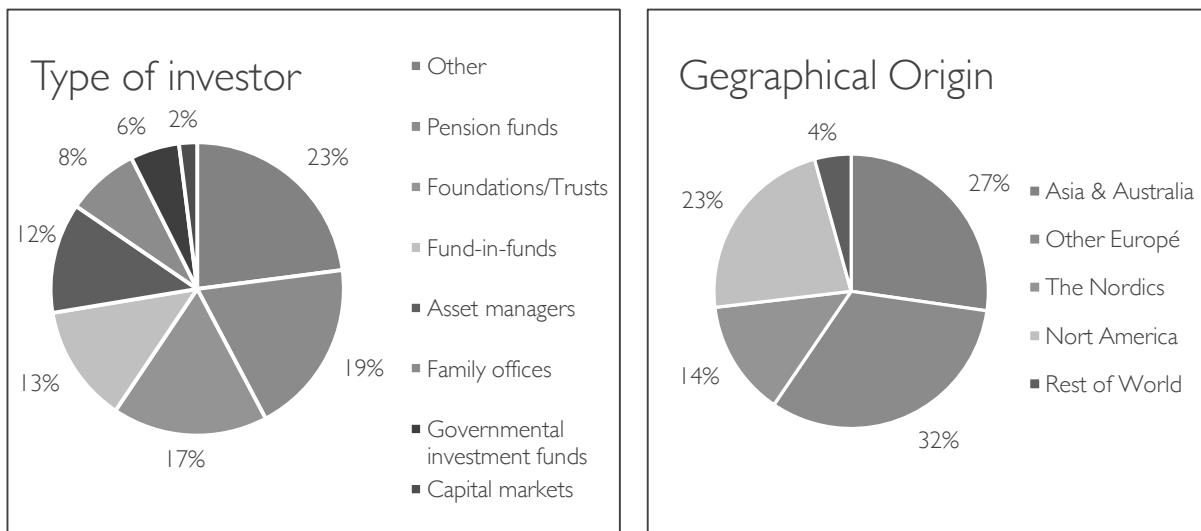


Figure 2: Origin of the invested capital in Sweden's commercial private equity companies (SVCA, 2014)

### 1.1.3 Risk Capital in the Swedish Media

Risk capital investors in general, and professional private equity companies in particular, are often targeted by criticism in the Swedish media. Some of the most common areas of critique include concerns that the investors are more concerned with cutting jobs and reaping short-term profits instead of developing their portfolio companies. Others question some private equity actors' tax-structures, whom use tax havens and aggressive tax planning to improve profits by reducing tax cost (Oral source/s, 2015-2016). Another topic that has been debated intensively is the risk capital's entry into public education and healthcare, which was fueled further by a scandal involving the risk capital owned healthcare company Carema in 2011 and 2012 (DN, 2012-2013).

All things considered, risk capital should be considered a relatively hot topic in the Swedish media. Why the following section will grant an initial research-based understanding of how the risk capital and private equity industry generally effects their portfolio companies.

Much of the critique states that private equity actors and private equity funds reduce the number of jobs in their portfolio companies when striving to cut cost, thereby impacting the society negatively (Oral source/s, 2015-2016). Since most of the new jobs are created in small and medium sized enterprises,

many private equity supporters therefore stress the fact that the private equity companies are in the forefront when creating jobs, due to the growth gained in their portfolio companies (Kellberg, 2015). When studied deeper, leading researchers discovered that a commercial private equity ownership lead to a minor and somewhat negligible decrease in the net number of jobs in the portfolio companies, when compared to a control group (Davis, et al., 2011). At the same time, the researchers revealed that the overall productivity of the companies increased. The critique was therefore somewhat disproved, though it can neither be said that the private equity actors alone cause the increase number of jobs in smaller and medium sized companies (Frontier Economics Europe, 2013).

Others criticize the private equity actors' ability to generate any substantial long-term value in their portfolio companies, or that they are only able to increasing the market value of the portfolio companies through financial engineering. Financial engineering means that the profits of a company are maximized in order to grow the market value of a company, only by rearranging financial information in the company's balance sheet and income statement (Christensen, et al., 2011). Such financial engineering is sometimes made before selling a company to increase the valuation of the company that is to be sold. Some examples of such activities include allocating cost as non-recurring and selling operational assets only to lease them instead (Ollila, 2015). This was frequently done in the early years of the private equity industry. However, according to the leading management consulting firms McKinsey and Bain (Bain and Company, 2014), the increasing competition in the industry have forced investors to develop the companies further, demanding much more than financial engineering activities (Mullin & Panas, 2014). Earlier quick-flips (investments held less than three years) are replaced with longer investment horizons and a deeper focus on the development of the companies' profits. Either through a growth in sales, a reduction in cost, or a combination of the two. This is exemplified in figure 3 below, showing the increasing share of investments held for longer periods of time.

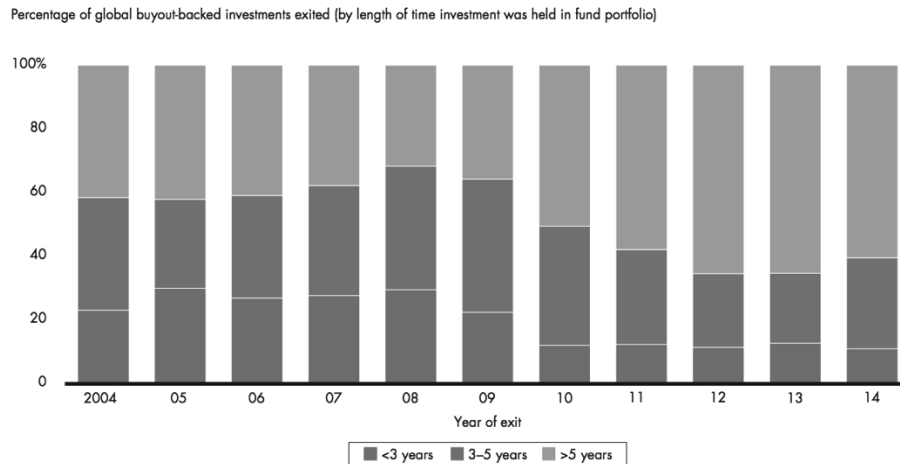


Figure 3: Length of ownership, global private equity funds (Bain and Company, 2014)

Investors are increasingly focusing on building long-term value, where innovations and the use of patents can be used as a proxy for determining the long-term investments made in a portfolio company. Researchers have found that there is generally no significant increase or decrease in the number of filed patents that is filed in the portfolio companies of private equity investors. However, the patents that are filed by private equity backed companies are generally much more cited than the others (Lerner, et al., 2008). They also discovered that the patents filed after an acquisition by a private equity company tend to be more focused. Therefore, they claim that the private equity investors do neither increase or decrease the efforts of a portfolio companies RnD department. Instead they force it to refocus on the areas that are expected to generate the value (Lerner, et al., 2008).

In summary, there is a heated debate in the Swedish media regarding the private equity industry's effect on the society and industry. However, when examining the research made in the field it becomes clear that much of the critique is somewhat unjust. With that said, the focus of much of the research made has been on the commercial private equity actors, and on buy-out funds in particular. There is somewhat of a gap regarding the privately owned investment companies within private equity. Therefore, more research is needed within the field to determine if there are any differences between the two categories, and if such differences is effecting their portfolio companies. This research gap is the one of the main reasons behind this thesis, which focuses on the Swedish privately controlled private equity sector.

## 1.2 Defining Risk Capital and Private Equity

The investment industry is highly complex, where investment actors and practices varies greatly between investors. Due to this complexity, a distinction will be made between the different major investment methodologies, and actors in risk capital and private equity. The focus will be on the different types of private equity actors developing companies through active ownership. Which excludes passive investors and investments made into publicly listed companies. Active ownership is defined in this report as: an investor that own a significant stake of the company and personally or jointly lead the development of the company. In the following section these actors are first categorized based on their investment practice, which is then followed by a section describing the different private equity actors within enterprise equity further. Ultimately an alternative categorization is presented which is based on the characteristics and motives of the investor, rather than its investment practice.

### 1.2.1 Different Types of Investments

The following categorization of investors is aimed at defining and distinguishing some of the most common investors that develop companies through active ownership. The focus of this report is on private equity investors within enterprise equity, why the actors in this group will be presented more thoroughly. The structure of these actors can be found below in figure 4, where the focus areas of this report are highlighted.

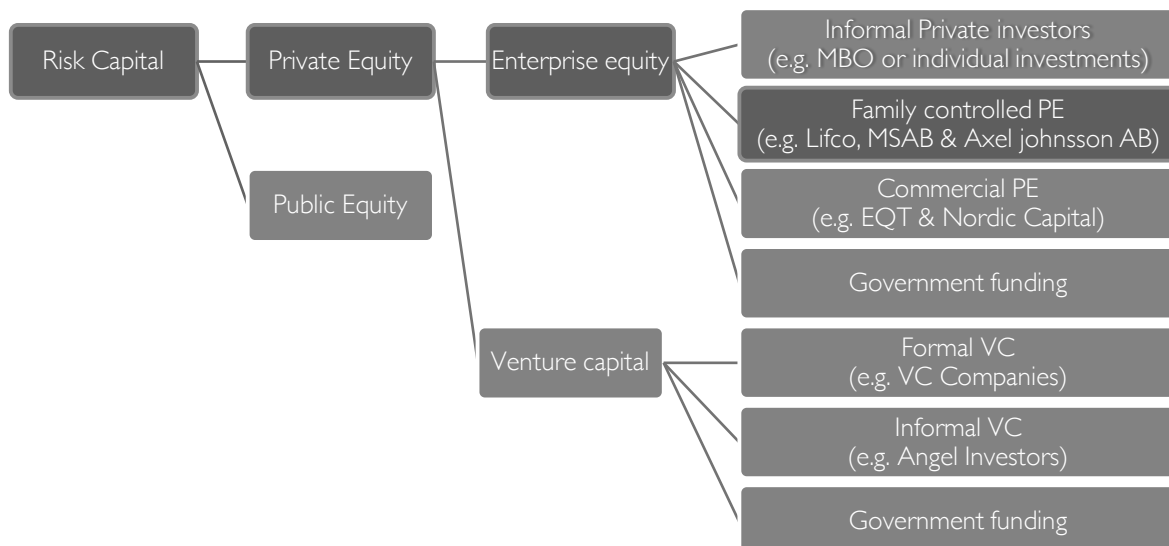


Figure 4: Different risk capital actors

### 1.2.1.1 Risk Capital

There are different ways in which a firm can be financed, in length meaning that there are several ways for an investor to invest in a company. The company can be financed either through debt, risk capital or a combination of the two, where both options include an abundance of different sorts of financial options. Debt capital include all sorts of debt accessible to a company, where the most common and simple sort of financing is through bank loans or credits. Risk capital can be defined broadly as all sorts of capital used to finance risky investments, however, in the academia, risk capital mainly means equity capital or an investment in exchange for ownership. This narrow definition is the one that will be used throughout the report (Isaksson, 2006). Risk capital therefore means that the investor takes on high degrees of risk correlated to the success of the company, risking the majority of the investment in the case of a default. Private equity actors primarily deal with risk capital, however, they often co-finance their investments by debt (EVCA, 2015).

### 1.2.1.2 Public and Private Equity

Risk capital can be used to invest in either publicly listed or private companies, called public or private equity. Hence public equity mainly refers to investments made in larger corporations through a stock exchange (Isaksson, 2006). Though in recent years' smaller stock markets and trade platforms such as "Aktietorget" have granted a platform for smaller firms to reap the benefits of public financing (Aktietorget, 2016). However, since the focus of this report is on private equity, public equity not be covered further. Private equity is defined by the European investment organization EVCA in the following way: "*Private equity is a form of equity investment into private companies not listed on the stock exchange.*" (EVCA, 2016) This definition is the one that will be used for the remainder of this report. It should be noted that the term private equity is sometimes used when discussing private equity funds, a type of commercial private equity company (Oral source/s, 2015-2016). The type of investor will be covered further in the following section, and will be referred to as commercial private equity, or private equity funds during the remainder of this report.

### 1.2.1.3 Different Types of Private Equity

There are many different types of private equity investors. These can generally be divided into two groups based on their investment practices and whether they invest in mature companies or new ventures (EVCA, 2016). These two groups are: venture capital and enterprise capital.



Venture capital (VC) includes all private equity investments that are made in the earlier stages of a company, such as seed capital, and early stage growth capital. These investments are often made in young start-ups and entrepreneur-led companies, typically driven by technological innovation (Laufer, et al., 2016). VC investments are often made by either professional VC companies, angel investors, governmental organizations or research/university related incubators and investors. VC investors are generally highly involved in the development of the company, working tightly together with the entrepreneur (Isaksson, 2006).

Enterprise equity includes all other forms of private equity investments made in more established firms. Where these firms range from small and medium sized enterprises (SMEs), to some of the larger companies in the world. The purpose of enterprise investments is often to grow, develop or turn a company around (EVCA, 2015). This category also includes buy-outs, meaning investments in publicly listed company, where the investor buys all of, or the majority of the stock and de-list the company. Where the result is a privately owned company. Buy-outs can also refer to management buy-outs (MBOs), where the management of a company buys the company from the previous owners (EVCA, 2015).

There are several different types of investors investing in enterprise capital, where some of the most notable ones are: informal private investors, family controlled PE (such as *Axel Johnsson Invest*, or Carl Bennet's *Lifco*), commercial private equity companies (such as private equity funds or listed private equity companies) and government funding (such as *Almi Invest*) (Oral source/s, 2015-2016). These categories will be presented separately with the purpose of granting a better understanding of the industry's different actors and the characteristics for each type of investor.

### 1.3 The Different Private Equity Actors

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This section will further describe some of the key actors within private equity, which were presented in figure 4. Since the actors within each category can differ greatly, the focus of this section is to grant the reader a broad and general understanding of the different actors, rather than an in depth and comprehensive description for each type.

### 1.3.1 Informal Private Investors

The private investors are a very broad and varied group, consisting of all individuals working with investments either privately or as a part of a smaller private investment company. They primarily invest their own capital, with an investment strategy often reflecting their previous job history or experience. This category includes actors such as business angels investing in enterprise equity and small private investment companies. Many private investors are previous managers utilizing their management experiences when investing in and developing new companies or ventures (Oral source/s, 2015-2016). In general, these private investors tend to be smaller than the other private equity investors, where the smaller amount of capital invested often differentiates them from other investors. The group is very heterogenic, why they are very hard to research and describe generically, which is hindered further by the fact that many intentionally wish to act discretely (Laufer, et al., 2016).

### 1.3.2 Family Controlled Private Equity

Another type of private investor that have a very dominant position in the Swedish economy is the family controlled private equity firms (sometimes called spheres). The firms are often named after the company's founder, generally investing the capital gained by the successful career as an entrepreneur, investor or manager. Some examples of such companies include Axel Johnsson AB, Melker Schörling AB and Carl Bennet's Lifco. These all stand out as privately controlled private equity actors actively developing their company (Oral source/s, 2015-2016).

It can be hard to distinguish the two sorts of privately controlled private equity groups mentioned. Therefore, as a rule of thumb, the larger most notable Swedish privately controlled private equity investors should be considered family controlled private equity during the course of this report.

Both of these private investment actors generally differs greatly from the commercial private equity actors, where the private investors can have different goals than the commercial actors. The fundamental goal of maximizing shareholder value is generally present for all investors, however, this goal can sometimes have a lower priority when compared to their commercial counterparts. For the private investors, other values such as growing or nurturing a portfolio company or its surrounding society can be of great importance. Where the investors may also favor keeping the control of the company within the family, sometimes even investing in projects that are of personal interest to the owners. This personal attachment grants another

level of complexity to the private investment companies, then for the commercial investors (Oral source/s, 2015-2016). Due to the heterogeneity among the private investors, it is difficult to state any generic descriptions for the companies (Laufer, et al., 2016). Furthermore, heterogeneity might be the reason to why less research has been made regarding the private investors, which proves the difficulties of successfully studying private investors.

### 1.3.3 Professional Private Equity Firms

When discussed or mentioned in the media, the term private equity is most often associated with private equity fund companies, however, the term covers a wide range of different sorts of private equity companies.

Traditional private equity firms are most commonly organized as a private equity fund, managed by a commercial private equity company. The funds' capital is typically raised from institutional investors, pension funds, banks and wealthy individuals. The capital is then locked for a period of time, called the vesting period of the fund, which grants the fund managers time to invest the capital as they seem fit. The vesting period typically ranges from 10-15 years but differ between companies. During the vesting period the original investors have a very limited say regarding the management of the fund. The fund-managers will typically charge the investors a fee for managing the fund. A fee that is typically set as a percentage share of the capital managed, as well as a share of the profits generated when divesting the fund. Some examples of the most prominent Swedish private equity funds include EQT, Nordic Capital, Segulah, Litorina, Procuritas and IK Investment partners.

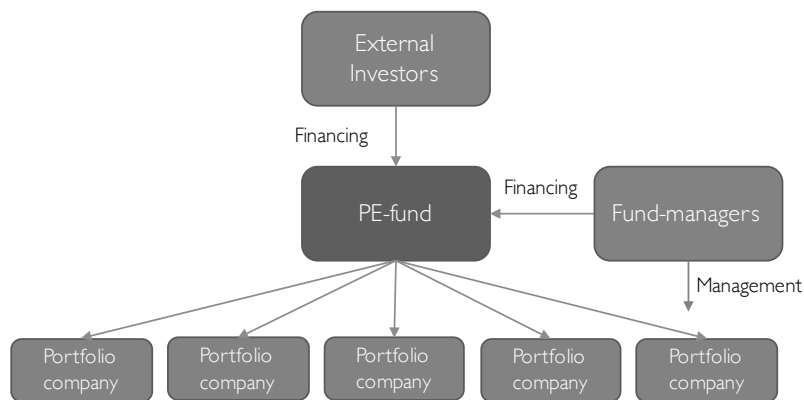


Figure 5: Traditional PE-fund structure [author's own illustration based on (SVCA, 2016)]

There are other types of private equity companies that operate without a fund-structure, with a specific vesting period. Instead they invest their capital continuously, called through something called an evergreen structure (Bain and Company, 2014). These investment companies can raise capital in a number of different ways, either through debt or equity products (such as loans or stock). One example of a Swedish evergreen private equity firm is Ratos, that is publically traded on NASDAQ Stockholm (Ratos, 2016).

Regardless of the structure of the private equity firm, they generally develop their portfolio companies aggressively to raise the companies' value. The involvement of the firms differs as much as the investors do, but some of the most common actions performed include exchanging key managers or board members, enabling financing, cutting cost and rationalizing bound capital (Oral source/s, 2015-2016). Since the competition in the industry is increasing, more focus is being put on the industrial development of the portfolio companies, rather than only relying on financial engineering (Christensen, et al., 2011).

One key difference between the private equity actors is their investment strategy. The firms' investment strategies can be more or less defined, where some firms have clear preferences regarding the types of companies in which they are looking to invest, where others have a broader scope (Oral source/s, 2015-2016). Some of the areas that are most frequently covered in these investment strategies include (SVCA, 2016):

- The size of the portfolio company
- If the investor seeks to invest in growth or turn-around companies
- The planned holding period of the
- What industries are to be invested in
- If they seek to control a majority or minority share of the company
- How much debt that is used to cover the investment

In general, the larger commercial Swedish private equity firms target a broad range of industries within Sweden or the Nordics and have a diverse portfolio of companies. The investments are often highly leveraged using high amounts of debt capital. The investments are commonly held for 3-7 years (SVCA, 2016). Thereafter, they are generally sold to another an industrial/strategic investor, made public via an IPO or sold to another financial investor seeking to develop the company further (Oral source/s, 2015-2016). The chosen route is most commonly based on getting the best price available for the company, thereby maximizing their return on investment (SVCA, 2016).

With that said there are a lot of greatly different private equity companies that instead focus on a specific industry or practice. Where the number of Swedish actors focusing on a specific industry have grown in recent years, much due to the increased number of generalized investors. Some examples of industries that are commonly focused on are currently: life-science, clean-tech and fin-tech (Oral source/s, 2015-2016).

### 1.3.4 Government Funding

In many countries, there are governmental actors support the industry with risk capital, competence and support. In Sweden, these actors' main purpose is to assist growth companies with risk capital and support, preferably in segments where the private capital is less inclined to invest. The private capital very much depends on the state of the global and national economy, as well as the governing investment trends. Due to these fluctuations one of the main purposes of the government activities is to stabilizing the availability of venture and risk capital over time (Riksrevisionen, 2014).

In Sweden, (according to data from 2014) there were primarily four state-financed actors within risk capital and private equity, these are: Almi Företagspartner AB, Fouriertransform AB, Inlandsinnovation AB and the foundation Industrifonden. Additionally, there are a number of regional companies that are co-financed by the government and also provide risk capital. In total, these companies controlled around 10 BSEK in 2014. Unlike their private counterparts these actors are not only driven by financial interests, why they are more likely to take on riskier investments. They are therefore often focused on early seed and venture capital, in ventures deemed too risky by most private investors. Another part of their investment strategy is that they often seek to find co-investors, such as private entrepreneurs, business angels or investors. Granting the company access to the competence and experience of the co-investor, whom often have invaluable contacts and networks (Riksrevisionen, 2014).

## 1.4 Problem formulation

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The private equity industry has been growing at a high pace both globally and in Sweden, why the sector is growing in importance for the Swedish industry. Many researchers have attempted to investigate the drivers and impact that these new commercial actors have. However, very little research has been made on the adjacent private investment sector also investing in private equity

cases. It therefore exists several research gaps regarding how these companies develop their portfolio companies and in length, what differences may exist between the groups. Insights that could be used to understand the different impact that the private investors have on the develop companies and the surrounding society. A topic that has been determined to be the cause of heated debate throughout the industry and in the media.

Therefore, this explorative thesis aims to shed some light on the discrete and relatively un-researched private investment sector, and their actions when developing private equity companies. Where the goal of the thesis is to gather knowledge that be used to accelerate future research within the field, and share insights with others interested in business development.

## 1.5 Purpose

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The purpose:

To analyze how private investors act, when transforming acquired companies through active ownership. Including the tools that are used, their development rational and the development process.

Research Goals:

- To establish a framework that can be used to analyze private investors
- To generate insights regarding private investors development process

## 1.6 Delimitations

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The focus of this study is on Swedish private/family controlled investment companies within private equity, that develop their portfolio companies through active ownership. Hence, any other types of investors are excluded in this study, even though the theoretical framework can potentially be used to study other investors as well.

Furthermore, the thesis will study one selected investment company, and its actions in four of its portfolio companies. No other companies will be studied as a part of this case study. The study will primarily focus on the development made during the first five years after having acquired a portfolio company.

## 2 METHODOLOGY

### 2.1 Research method

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This study has been performed using a combination of theoretical and empirical data. In the initial stage of this thesis, a literature study was performed, granting a deeper understanding of the industry, the industry's different actors and the practices used. Thereafter, initial interviews were made with individuals with extensive experience from the industry. Additionally, a number of conferences and seminars were attended by the author, granting further insights into the industry and the development methodologies used by private equity investors (Eriksson & Wiedersheim-Paul, 2014).

After having performed the initial investigation, a qualitative case study was conducted. One of Sweden's larger private/family controlled investment companies within the private equity sector was selected for this study. Four of the investment company's portfolio companies were selected to partake in the study, with the goal of examining both the characteristics of the investment company and the development made in its portfolio companies. The companies were examined using semi-structured deep interviews with: senior management, the board of directors and investors. These interviews were complemented with an archive analysis based on documentation from board meetings, investment strategies and other forms of available material. Furthermore, observations were made by the author, when gathering data at the investment company. Thereafter, the gathered data regarding the investment company and its portfolio companies were compiled and discussed with representatives from the investment company, to ensure the reliability of the data. This compilation was used when analyzing the material, forming the conclusion and development process used by the investment company (Eriksson & Wiedersheim-Paul, 2014).

## 2.2 Research process

For this study, a research process consisting of 9 steps was used, which can be found in the following illustration. The process was designed to ensure sufficient insights into the field, before initiating the case study. In the following section, these steps will briefly be presented.

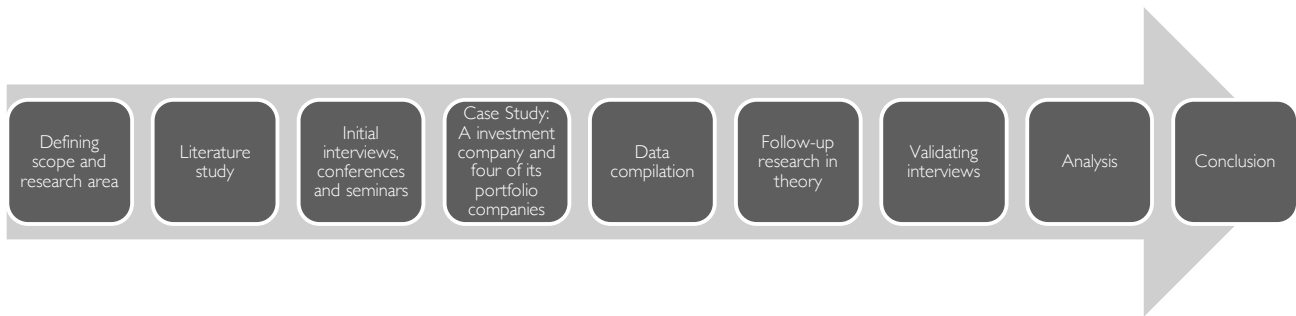


Figure 6: The research process

### **Defining scope and research area**

In the first phase of the study, the scope and research area was selected. The private/family controlled section of the private equity industry was selected for research, due to the lacking amount of publications within the area.

### **Literature study**

A literature study was conducted in order to grant the study and the author deeper insights into the field. The study investigates company development, the investment sector in general and the private equity industry in particular, why literature for these fields were examined. The publications, books and articles were found using a combination of Lund University's databases, leading papers and reviews, and highly cited research papers within the field.

### **Initial interviews, conferences and seminars**

To further grant insights into the field, a number of seminars and conferences were visited by the author. These were focused on the fields: private equity, corporate governance and the work of board of directors. In total two seminars were attended, one conference regarding M&A, one training program for board of directors. Furthermore, four external interviews were held with industry experts.

### **Case Study: A investment company and four of its portfolio companies**

During the case study, one investment company was studied, where a number of interviews were conducted with different investors at the firm. Thereafter,



four of its portfolio companies were selected to be used as further case studies. The companies were selected based on similarity and size, where the aim was to select four companies with similar characteristics but different size, measured in turnover. These companies were studied using semi-structured deep interviews and a total of 9 interviews were held with people with connection to one or several of the investment company or portfolio companies.

#### **Follow-up research in theory**

In this section additional theory was added to the theory section in order to successfully cover all aspects examined in the empirical data. Where some additions were needed due to the specific development practices of the studied company.

#### **Data compilation**

The empirical data was thereafter compiled, in a manner best suited for comparison with the theoretical data, and for identifying similarities or differences between the developed companies.

#### **Validating interviews**

After compiling the data, one final round of interviews was performed to ensure the reliability of the data. Where the focus of these interviews was to ensure that no actions were missed during the initial study.

#### **Analysis**

In the analysis, the empirical and theoretical data was analyzed, and a number of similarities and differences were identified. Thereafter the empirical data was used to develop a set of development stages, based on the development characteristics of the investment company.

#### **Conclusion**

The conclusion was thereafter based on the key findings from the thesis, where the findings mainly consists of the development process and other areas discussed in the third and fourth analysis section.

## 2.3 Research strategy

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In this section, the rational for the selected methodology is presented, combined with an explanation of some of the different available methodology options. Additionally, the reasoning for selecting the studied investment

company and its portfolio companies will also be discussed in this section (Eriksson & Wiedersheim-Paul, 2014).

### 2.3.1 Explorative and Descriptive Study

Within the field of private equity and business development, much research has been made. However, within the private/family controlled investment sector, very limited research has been published. Since this study aims to investigate this poorly researched area, an explorative study is selected (Höst, et al., 2006). Explorative and descriptive studies are best suited for areas in which relatively little research has been made, why it suits this specific area of the private equity sector well (Eriksson & Wiedersheim-Paul, 2014).

### 2.3.2 The Investment Company and its Portfolio Companies

This master thesis studies the private/family controlled private equity industry, by examining one specific private investment company. Due to the scope and limitations of this study, it was determined that studying one investment company extensively would grant better results than a shallower investigation of multiple investment companies, why one investment company was selected (Höst, et al., 2006). The investment company was selected partially based on the author's previous relationship with the investors, which allowed access to critical and confidential information. Another reason for selecting the studied investment company is its strong track record. The company has continuously outperformed the industry average, and is now considered by many professionals within the area to be one of Sweden's most successful private investment companies.

Four of the investment company's portfolio companies were selected, portfolio companies that were chosen to best demonstrate the earlier development process made by the investment company. The criteria used when selecting these portfolio companies include: value growth, different industries, time of acquirement, maturity and size. For the growth criteria, increased margins and turnover was used as basis of measurement. A combination of different companies was selected, consisting of a combination of successful companies and companies that are still under development. Time of acquirement was used to ensure the time-relevance of the acquired companies. Where the companies selected were required to have been owned for more than 1,5 years, ensuring that the investment company would have had time to initiate changes in the companies. The industry criteria was used

to ensure that the companies represented different industries, increasing the generalizability of the results. The maturity and size criteria were used to select similarly sized companies that had reached a relatively mature development stage. Why entrepreneurial and early growth companies were excluded. Specifically, the selected companies were required to have a turnover of between 150 and 600 MSEK at the time of the acquisition.

### 2.3.3 The Selection of a Qualitative Methodology

When performing a case study, there are two different types of research methods that can be used: the quantitative and qualitative method. The quantitative method relies on numbers, statistics and generally large amounts of data, in order to perform a numerical analysis. The qualitative research method instead relies on a more focused analysis, where interviewees are asked to explain their interpretation and experiences regarding the subject. A qualitative research method is best suited when researching a subject that can be hard to classify and quantify (Eriksson & Wiedersheim-Paul, 2014). Qualitative further allow the researcher to adjust the method during the course of the study. Thereby allowing the exploration of previously unknown aspects of the topic. A quantitative method is ill suited for such flexibility due to its requirement of structured quantifiable data. Since the study is explorative and aimed at understanding a complex and poorly researched, a qualitative method is chosen (Holme & Solvang, 1991).

### 2.3.4 Multiple and Single Case Study

Case studies are used to investigate and understand one specific phenomenon or object, and is best suited when researching an object that is hard to separate from its surroundings, or compare to its peers. Case studies can be performed by their own or as a comparison between two or more studied objects, a so called multiple case study. A combination of a single and multiple case study is used in this thesis. For the investment company, a single case study is performed. However, this single case study is performed by conducting a multiple case study of the investment company's portfolio companies. This mixture was selected to best investigate the characteristics of the specific investment company, where both the investment company and its development of its portfolio companies are subjects to this study (Höst, et al., 2006). When performing a case study qualitative data is often used, where three main sources of information are best suited for a case study: interviews, observations and archive analysis. A combination of all three is used in this study, where the main emphasis lies on the interviews with key actors from the investment company. The rationale for choosing all of the three methods

will be discussed below, as well as the need for flexibility when performing a case study (Eriksson & Wiedersheim-Paul, 2014).

#### 2.3.4.1 Interviews

When performing interviews, a number of different approaches can be used. The interviews can be structured, where questionnaires are used in a structured and repeated way, where the interviewer seldom complement the questionnaire with relating questions. The interviews can also be semi-structured, where a questionnaire is used as a basis of discussion and then followed-up with relating questions, to get further information about the subject. Furthermore, the approach can also be unstructured, where the interviewee is asked to answer open-ended questions, allowing him or her to steer the interview. In this study a combination of semi-structured and unstructured interviews is used. An approach that was chosen due to the subject's complexity and fairly unknown nature, where the interviewees were asked to elaborate on subjects that they thought would contribute the most to the study. Additionally, the semi-structured method ensures that the interviewees are asked to share their views on the same matters, which is crucial when validating their subjective insights regarding the different studied portfolio companies (Höst, et al., 2006).

#### 2.3.4.2 Observations and Archive Analysis

Other common research methods in a case study include observations and archive analysis. The two methods are generally used to ensure the validity of the data, by verifying what is said during the interviews. Due to the risk of receiving subjective answers during semi-structured and un-structured interviews, both observations and archive analysis was used. The observations were performed by the author while studying the material at the investment company. Thereby experiencing how the investment company work when developing portfolio companies and deciding to invest in new companies. Furthermore, the archive analysis was performed using any available documentation regarding the portfolio companies, that were either established by themselves or by a third party. This archive analysis came to include: board minutes, strategic documents, externally made market analysis and information gained during the due diligence process (Höst, et al., 2006).

#### 2.3.4.3 Flexibility

Case studies are often flexible, where the exact process method is seldom known in advance when performing the study. This flexibility can be beneficial since the methodology may need to be developed based on the information gained during the case study. This is particularly true when

performing an explorative study, where the unknown nature of the research area may require further development of the methodology (Eriksson & Wiedersheim-Paul, 2014). Another strength of a flexible study is the possibility to adjust and correct the data gained during the course of the study. Qualitative data can be misleading, due to its subjective nature, especially in a complex area. However, minor adjustments to the methodology can help prevent these misinterpretations, where a previously open question can be developed deeper based on the information gained throughout the study and from other interviewees (Höst, et al., 2006).

The research method in this study was refined throughout the course of the study due to the benefits of a flexible study when performing an explorative case study. The initially planned methodology was extended to include additional sources of data, with the purpose of increasing the relevance and quality of the study. Particularly, these changes include: a review of the theory section, the inclusion of additional external interviews and seminars and final validating interviews with key personnel from the investment company.

The seminars were primarily aimed at granting the author further insights into the work of an investor. The author attended a series of courses, where speakers with previous experiences from *The Swedish Academy of Board Directors* held training courses on the theme “the board of directors”. Additionally, a conference held by one of Sweden’s leading business magazines: *Dagens Industri*, was attended, where new trends within M&A and company development was discussed. Furthermore, additional seminars were attended regarding topics that were determined to be of value to the study.

## 2.4 Research Delimitations

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Research on private investors within private equity actors is limited, and the main sources of information regarding such actors cover larger, commercial private equity funds. The research papers often focus on larger American private equity funds, where differences in corporate culture and regulations often lead to significant differences when comparing these companies to their Swedish counterparts. The private Swedish companies are only required to publish very limited data on how they operate and how they are performing, which further hinders research within the area and the comparability between companies. Due to this lack of data one specific investment company was selected, which somewhat hinders the generalizability of the results of the study.

## 2.5 Method of Analysis

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The analysis was performed through an initial comparison between the theoretical and empirical data, in the first two sections of the analysis. This information was thereafter combined with the identification of the actions made in the different portfolio companies. This information was compiled into a Gantt-plot, where the duration and time of initiation of the different development actions, were used to find similarities and differences in the development of the companies. These differences were used to identify different development phases used in all of the companies, which was thereafter compiled into a generic development process. This process, combined with the overall findings of the analysis section was then used when forming the thesis' conclusion.

## 2.6 Reliability and validity

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Reliability refers to the research method's ability to generate the same results when performed more than once (Eriksson & Wiedersheim-Paul, 2014). Since this report relies heavily on subjective information and the authors interpretation of the subject, the reliability of the data cannot be assured. However, this error is reduced as much as possible through the usage of a broad range information, gained from the interviews, observations and archive analysis.

The validity of the research means its ability to accurately investigate the research area (Eriksson & Wiedersheim-Paul , 2014). The validity of the of the study is considered to be fairly strong, through the usage of multiple different sources, semi-structured interviews and a flexible methodology that was readjusted to best fit the research subject. Furthermore, the subjective data from the interviews was to a high extent validated through the usage of objective information, such as financial information and clarifying board minutes. Ultimately, the compiled information was on a number of occasions discussed with the studied company to ensure that no relevant information was left out.

It should be noted that a necessary source of data for this type of study is the confidential information and documentation shared by the board. Data that is often strictly confidential and closed to the public. This strict confidentiality hinders the comparison with other investment companies, and hardens the depth of data available. Within the field quantitative data is scarce, which

causes the data to be questionable due to its subjectivity and risk of being miss-interpreted. Furthermore, this confidentiality requires this study to be anonymized, why neither the investment company, nor its portfolio companies are presented by name.

# 3 THEORY

## 3.1 Introduction

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In order to analyze the work of investment companies, one must first get a holistic understanding of how an active investor can develop a portfolio company, and what tools are available. This theory chapter's section *Levels of Strategy* aims to grant an understanding of the different strategic options available to an investor when developing a portfolio company. These options are presented for each of the different levels: corporate level, business level, and functional level. Thereafter some key aspects for investigating an investor are presented in the section *The Investor's Perspective*. Together, these two sections grant a holistic understanding of the interactions made between an investment company and its portfolio company, when developing the portfolio company.

Before discussing these key areas, a basic introduction to the definition of strategy, corporate governance, the board of directors is presented and investment rational. The definition of strategy ensures shared understanding of the concept, which is necessary since it will be used extensively throughout the report. Thereafter a section covering corporate governance, the board of directors and investment rational is presented. This section aims to grant an understanding of the key stakeholders that govern a company, and the board's role in its development. The role of the board of directors is critical, since it often represents the main point of contact between the investor and the portfolio company. Ultimately, the investment rational covers some key aspects that distinguish different types of investors, which can influence their different development methodologies.

## 3.2 Definition of Strategy

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The concept of strategy must first be defined before discussing the model: levels of strategy. Strategy can simply be as the long term-orientation of an organization. However, the term does often have a much wider meaning, where the following definitions, or similar definitions of the two, are often used in the academia.

“Competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value.”

(Porter, 1996)



“Strategy is the direction and scope of an organization over the long-term: which achieves advantage for the organization through its configuration of resources within a challenging environment, to meet the needs of markets and to fulfil stakeholder expectations.”

(Johnson, et al., 2008)

This broader definition of strategy will be used when discussing the development of a company, which focuses on the activities that a company can initiate to generate value. The definition will be used as a guide when investigating the different levels of strategy.

### 3.3 Corporate governance

In Swedish companies, the corporate governance structure is regulated by the Swedish law “*Aktiebolagslagen*”, a law stating that the company is to be governed through four entities (Wiberg & Salomonson, 2010). These entities are shortly described below and are thereafter followed by an in depth description of the board of directors, due to the importance of the board when developing a company. It should be noted that the corporate governance of companies differs across the globe and due to the limitations of this report, only the Swedish model will be discussed. The four different entities of the Swedish corporate governance structure are:

1. The Annual Shareholder’s Meeting
2. The Board of Directors
3. The CEO
4. The Auditor

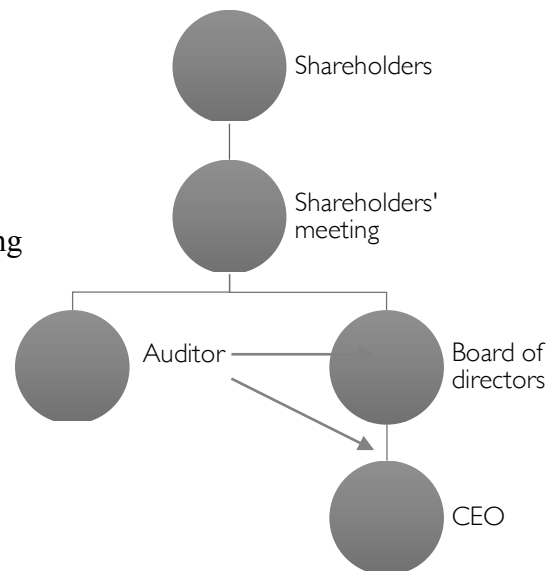


Figure 7: Swedish corporate governance (Wiberg & Salomonson, 2010)

During **the shareholders' meeting**, the shareholders determine several key areas regarding the governance of the company. Some of the most important aspects include: choosing the board of directors, the accountant, confirming the annual report, deciding on dividends for the shareholders and remuneration for the members of the board and the accountant. The meeting is required by law to occur at least once a year, or more if deemed necessary by the board. The meeting also decides whether or not to grant freedom of liability to the board and the CEO (Wiberg & Salomonson, 2010).

**The board** is responsible for governing the company between the shareholders' meetings on behalf of the shareholders. In private companies, the board needs to consist of at least one board member and one alternate member. Where a public company's board needs to consist of at least three board members. If the board consists of more than one member, one of them is required to be selected as the chairman of the board (Grant Thornton, A, 2015). The board is personally responsible for the governance of the company, ensuring that everything is in order. Which includes anything from formalities such as paying taxes and administrative costs, to the overall governance of company (Dansell, et al., 2014). Some of their most important tasks include: the selection of the CEO, the monitoring of the company, and the guidance of the company (Wiberg & Salomonson, 2010).

**The CEO** is responsible for the day-to-day operations of the company as well as ensuring that the accounting is done correctly. Which specifically mean that he or she is responsible for implementing the decisions that are made by the board. Furthermore, the CEO is expected to lead the company in a way best aligned with the wishes of the shareholders (Wiberg & Salomonson, 2010).

**The Auditor** works as the controlling function, ensuring the finances of the company and that the work of the CEO and board is done correctly. The auditor does also have an important role when recommending the shareholders to grant the CEO and the board of director's freedom of liability, or not. Regardless, the final decision is still made by the shareholders during the shareholders' meeting (Wiberg & Salomonson, 2010).

However, these roles are not always distinguished, since many companies (especially smaller ones), have the same people represented in many of the different different entities. One typical example is an entrepreneur-led company, where the majority shareholder is often both the chairman of the

board and the CEO of the company. This can hinder the entities from performing at their best, and represent one typical area where family or entrepreneurial led companies can often be improved (Grant Thornton, B, 2015).

### 3.4 The Board of Directors

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The Swedish corporate governance model requires companies to have a board. Where the board of directors is both responsible for some administrative duties and the strategic governance of the company. An effective board can increase the performance of a company, why some of the dynamics of the board are discussed in this section.

The board of directors are responsible for implementing the will of the shareholders, and are selected by the shareholders during the annual shareholders' meeting. The board's roll is mainly to **govern** and **control** the company, and represent one of the most critical parts of the corporate governance. When controlling the company, the board must ensure that the company complies with laws and regulations such as "*Aktiebolagslagen*" and the requirements that comes with it (Wiberg & Salomonson, 2010). Such formalities are a necessary part of the board's work, though are not deemed to have a significant impact on the development of the company, why they will not be discussed further in this report (Dansell, et al., 2014).

The **governance** aspect however, can have a huge impact on a company's performance. In general, it is through the board that investment companies influence their portfolio companies. Where some of the board's most critical decisions include: developing the organization's strategy, prioritizing activities, allocating resources and the recruitment of key senior executives. The selection of the CEO is often considered the most critical task of the board, though their duties can also include the recruitment of other members of the senior management team. Since the board work on behalf of the shareholders, it is up to them to handle the risk of the company when setting the strategy. Other critical areas toward the shareholders include information sharing and ensuring the transparency and reliability of reports to the shareholders (Wiberg & Salomonson, 2010).

The board should ideally consist of somewhere between 3-8 members, depending on the characteristics of the company. In smaller companies, the board is generally more effective when it consists of 3-5 members, where a larger company should instead have 5-8 members (Dansell, et al., 2014). One

of the major benefits of having fewer members in the board is that they will in theory be able to reach decisions faster, allowing them more time to tackle larger amounts of challenges. A larger board is instead better suited for more thorough discussions, allowing the board access to a wider range of competence, which can be beneficial when tackling tough strategic issues (Wiberg & Salomonson, 2010).

A professional board should be formed when the company grows beyond 15-20 employees, or earlier if company's surroundings is radically changing. Some examples of when a board should be formed earlier include: facing aggressive expansion, imminent change in ownership, or before a generation shift (Grant Thornton, A, 2015). A professional board ideally consist of a mixture between internal and external board members that have the competence needed for the upcoming challenges of the company (Dansell, et al., 2014). External board members can often help increase the efficiency of the work done by the board, where professional external board members can help the board to focus on the most critical issues at hand (Andersson, et al., 2010). They can often help reduce the time spent on routine reporting, unlocking more time to be spent on strategic challenges and value creating decisions (Wiberg & Salomonson, 2010). According to to the researcher Kent Sahlgren at Gotherburg university external board members often help increase the efficiency in the board. Which if combined with an active follow-up and goal setting, can help companies increase their turnover by as much as 280 %. The value of including external board members in the board is agreed upon by many researchers and professional managers. Where the famous Swedish business man Ulf Spendrup claims the following (Dansell, et al., 2014):

“The family-owned companies that do not have external board members in their boards of directors miss out on great value.”

There are alternatives to having external board members if the company wants to get input externally without changing the members of the board. Some of the most common alternatives include hiring consultants, creating and advisory board, or through the use of alternate board members. Alternate board members can be a great way to test how new potential board members where to fit in the current board, as well as gaining access to a set of competence for a limited amount of time. The rest of the alternatives can be highly beneficial, though tend to be costly (Grant Thornton, A, 2015).

In a survey performed by the research institute Mistat AB in 2014, where 1550 representatives of Swedish entrepreneur-led companies responded, only 54 % claimed to have an active board. Where only 36 % of the respondents claimed to have a good or very good mixture of internal and external board members. The respondents were selected based on their roles as CEO, CFO, shareholder or member of the board, and the survey had a 21 % response rate (Dansell, et al., 2014). The survey clearly shows that there is a lot of room for improvement in smaller Swedish entrepreneur-led companies, a development potential that can help explain why investors are often successful when transforming companies. Since the investors act as external board members, often with vast experience from other companies, that grant the companies external input (Grant Thornton, A, 2015).

### 3.5 Investment rational: Industrial, Financial and Private Investors

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Another way of categorizing investors is based on the motives and characteristics of the investor, Within the investment industry, investors are often separated in the three groups: financial investors, industrial investors and private investors. This grouping is used throughout this report referencing to other adjacent types of investors that can have an impact of the portfolio companies (PWC, 2015).

Financial investors include professional investors working in or with connections to the financial sector. This group include, but is not limited to: investment and commercial banks, private equity funds and venture capital firms. The firms differ though they have similar practices and focus heavily on maximizing shareholder value (PWC, 2015).

Industrial investors include investors that opt to invest in a company to benefit their corporate parent. This group can also be called strategic investors, since the investor or corporate parent is often a large industrial firm seeking to develop the portfolio company as a part of the industrial group. Some of the most common reasons for an industrial investor seeking to invest are: acquiring patents, gaining access to new markets, acquiring market share or new technologies (PWC, 2015).

The final group, private investors, refers to all investments made by an individual or a small group of people, investing their own capital. Due to the diverse nature of the group it is hard to define their key characteristics. However, some of the most common sorts of private investors include: managers participating in a management buy-out, private or family controlled investment companies, angel investors, or other wealthy individuals. This categorization is very blunt and not very precise, however, it easily grants an initial indication to the motives and characteristics of the investor (PWC, 2015).

## 3.6 Levels of strategy

Strategies exist at all levels of any organization, ranging from the overall corporate strategy, to specific goals for individuals or teams. In the model “Levels of strategy”, these are split into three main groups: corporate strategy, business strategy, and functional strategy. These levels will be presented further in this section, and are used to organize managerial tools and methods used when developing a company. The tools presented focus on their effect on the developed portfolio company. Hence, the corporate parent, or investment company, will much be excluded in this section. Factors regarding the investment company will instead be discussed in another section.

*It should be noted that the majority of the information presented in this section has been retrieved from the five commonly cited strategy books: (Johnson, et al., 2008; Barney, 2011; Ireland, et al., 2009; Barney & Hesterly, 2015; Grant, 2005). All of these books are not always referred too due to editorial reasons, instead many references are made for the most cited work: (Johnson, et al., 2008), that can be seen as an example case for these different standardized strategy books.*

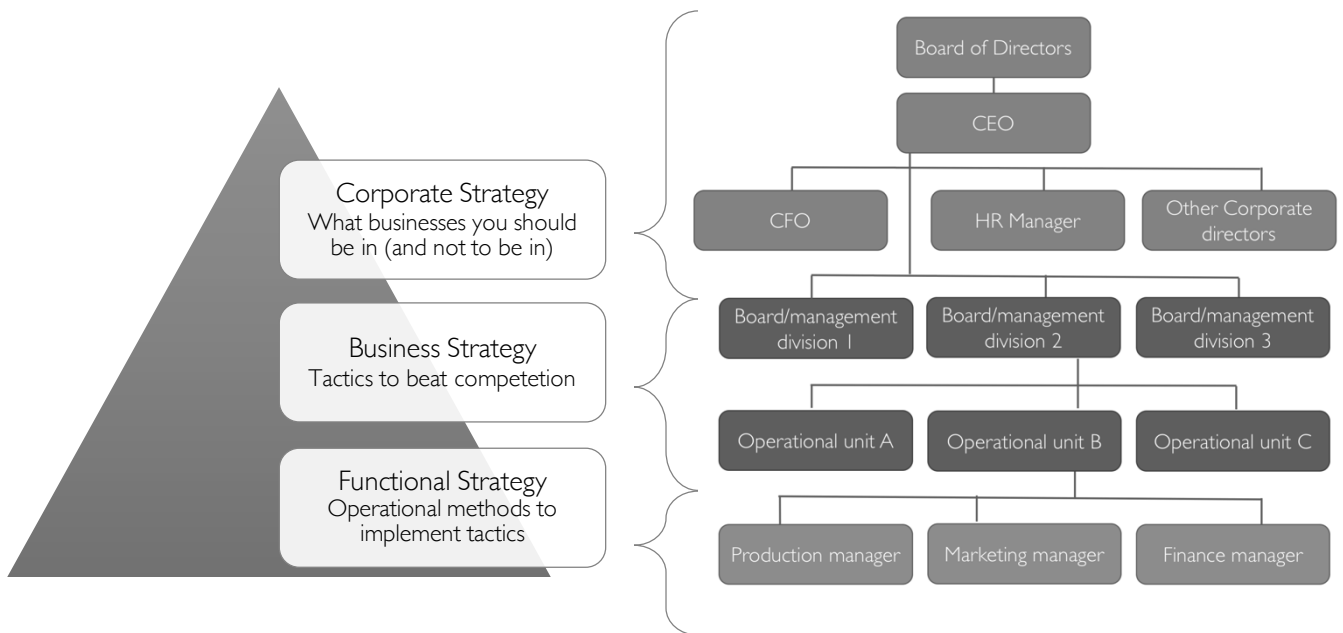


Figure 8: The Levels of Strategy (Johnson, et al., 2008), and its corresponding levels at a standardized organization

**The corporate strategy** concerns the overall strategy, or the strategy set at group level, determining the future of the company. The corporate strategy is often set by the board of directors and c-suite management and is often influenced by the shareholders (Johnson, et al., 2008).

**The business strategy** determines the goals for a specific business unit, which could be defined as a regional office, product category, or any other categorization used by the company. The business strategy is set by the management team for each individual business unit, with guidance granted by the corporate strategy. Depending on the size of the company it may be hard to separate the business and corporate strategy, where the two are often tightly linked in small and medium sized companies (Johnson, et al., 2008).

**The functional strategy** is set to guide all functions of the company, specifying performance goals and processes. Some examples of such functions include the departments that are responsible for: supply chain management, marketing and sales, or human resources. The strategy is often set by departments' individual managers, whom are often a part of the management team that set the business strategy for the entire business unit (Johnson, et al., 2008).

These three levels of strategy, will be discussed extensively in the following sections. Granting a deeper understanding of each level, and how they can be tackled by an investor seeking to develop a company (Johnson, et al., 2008).

### 3.6.1 Corporate Strategy

The corporate strategy is concerned with the overall scope and purpose of the company, determining how the firm is to best align its business units. The corporate strategy covers all of the mayor decisions a company makes, such as: what and how products and services are offered, geographical coverage and how resources are allocated. This critical level is mainly influenced by the company's investors, board of directors, shareholders and top directors, often expressed in a mission statement and strategic plan (Barney, 2011).

There are a number of different strategies that can be implemented when developing a company (Ireland, et al., 2009). Some of these are presented in this section, where an overview of the section is found in the following list. These strategies will be used as a foundation when investigating how investment companies acts in relation to the portfolio company's corporate strategy. Furthermore, the resource based view is presented, a model and



method of analysis when evaluating a firm's core capabilities and/or competences (Johnson, et al., 2008).

- ✓ Diversification strategies
- ✓ Vertical Integration
- ✓ Strategic Alliances
- ✓ Mergers and acquisitions
- ✓ Resource based view

#### 3.6.1.1 Diversifications strategies

Implementing a diversification strategy means that a company diversifies itself by broadening its product portfolio, or by entering multiple markets or segments. The model classifies an organization targeting multiple markets as market diversified. Where an organization seeking to broaden its product offering is called product-diversified. A company can implement both strategies at the same time, thereby becoming market-product-diversified (Johnson, et al., 2008).

Diversification strategies have been used to a varying extent during the last decades and was very popular until the 1980's. Large businesses sought to diversify themselves into large conglomerates, however, only a few of these conglomerates benefited from this aggressive diversification strategy. It soon became evident that not only rational motives drove these diversifications, where the two negative drivers: overconfidence and managerial hubris are often considered to explain some of the irrational reasoning (Barney, 2011). Since the 80's the number of conglomerates have declined, where many corporations have been forced to focus on their core competences and strategic fit (Oral source/s, 2015-2016). However, there are still a lot of diversified conglomerates, especially in emerging markets; such as Asia Pacific and Latin America (Johnson, et al., 2008).

Diversification is driven by three main drivers: growth, risk reduction and profitability. Growth can successfully be reached through add-on acquisitions or mergers. However, such growth is sometimes acquired at the expense of profitability, reducing shareholder value. It is therefore important to evaluate the importance of such growth, where ill implemented growth investments risk destroying shareholder value. When seeking to decrease risk, a diversification strategy can be successful when spreading the risk of a company over multiple business units, geographical markets, or products. Which can be highly beneficial for companies in industries that are characterized by high cyclicity, high investment requirements, or

companies relying on a low number of segments (Barney, 2011). The final driver, profitability, refers to the strategy's ability to reach synergy gains or advantages when expanding its offering (Johnson, et al., 2008).

According to Porter, a diversification strategy should be implemented if the expected profits, plus a risk premium, exceeds the cost of implementing the strategy. This may seem self-explanatory, but many conglomerates have grown beyond reason, due to factors such as managerial hubris or personal gains, why the financials and projections of the initiative must be evaluated carefully (Johnson, et al., 2008). Another reason for irrational diversification is thought to be some managers' intent to decrease the company's risk, driven by their will to ensure their job security. However, such risk aversion should be initiated by the investors, rather than the managers, since shareholders seldom benefit from such behavior. The transaction costs for an investor diversifying his or her investment portfolio is much lower than the cost of diversifying each individual investment. Therefore, the goals of the shareholders and managers need to be aligned to reduce the risk of them counteracting each other (Johnson, et al., 2008). This is one part of the so-called agency problem, that will be described further during the section *the investor's perspective* (Eisenhardt, 1989).

#### 3.6.1.2 Vertical integration

Vertical integration is a strategy relating to the company's presence in the value chain. When a company implements vertical integration, it will pursue a broader and more dominant stance in the value chain. The strategy can be achieved either through forward or backward integration (Johnson, et al., 2008). Forward integration means that firms further down the value chain are acquired, which brings the company closer to its end consumer. Backward integration instead means that a firm's suppliers are acquired, granting the firm more control over its production capabilities. Such backward integration is often implemented by car manufacturers, that acquire suppliers to get access to ensure their access to critical components or technology (Barney & Hesterly, 2015).

There are both pros and cons connected with vertical integration, though industries generally tend to integrate at an increasing rate. This is clearly demonstrated when examining the industrial output in the United States. The share of the total output generated by their 100 largest companies was around 35 % in 1928 and grew to around 65 % in 1998 (Grant, 2005). This radical change is driven by several drivers, where two of the strongest ones are lowered transportation cost and the consolidation of profits. Consolidated

profits can help a company to keep their prices down, locking other customers out. One critical aspect of the lowered transportation costs is the possibility to co-localize key facilities within close proximity of each other. Co-localization is frequently implemented in the mining industry. Where mining companies co-localize mines and production plants to eliminate expensive transportation of heavy, unprocessed ore (Grant, 2005).

Some factors that needs to be considered when evaluating vertical integration is: the scale of the operations, the need to be flexible, risk management and how incentives are organized. When integrating, the scale of the operation should be large enough to be motivated by scales of economics. Why many small niche actors never reach an operational scale large enough to motivate vertical integration (Grant, 2005). Instead, such actors may benefit more from working tightly with a network of suppliers. One downside of vertical integrating is the loss of flexibility, where an unintegrated company is more flexible since it ca switch between suppliers. An integrated company is also subject to higher degrees of risk, since larger parts of the value chain becomes exposed (Johnson, et al., 2008). The final aspect concerns how the companies' incentives are organized. When operating as separate suppliers, the performance targets of the business units are often very clear, where the companies' profits can be easily monitored and developed. In an integrated business unit those drivers may instead be hidden by the larger corporation's bureaucracy, which risk leading to deteriorating performance. However, the opposite may also be true, where a large effective company may grant the smaller business unit synergies, granting a more efficient business (Barney & Hesterly, 2015).

### 3.6.1.3 Strategic alliances

Companies can benefit greatly from cooperating with other firms in all areas of their value chain. Some of these benefits have been discussed in the vertical integration section, as well as during the M&A section. However, a firm can not only gain access to these benefits through acquisitions or organic growth, but through partnerships and strategic alliances as well. Instead of being owned jointly, firms can coordinate their efforts through partnerships, thereby getting access to the information and capabilities available to each of the different companies. There are many different sorts of these types of partnerships, where three of the most common ones are presented in this section: Long term contracts, vendor partnerships and franchising (Johnson, et al., 2008).

#### Long term contracts

One type of partnership is the co-signing of long term contracts. Here the parties often agree to buy and/or sell a set of items over a period of time, rather than performing one transaction at a time. The agreement facilitates the transaction process since the terms are predetermined which does not require the buyer to reassess their suppliers before each purchase. Therefore, the agreement can grant the parties long term benefits, where less time and resources are spent on transaction costs (Barney & Hesterly, 2015). Which can allow the supplier to better optimize their production and delivery planning. From the experiences gained by working together, new routines and process can be established, and in length potentially reducing cost. However, many problems can occur due to differences that the parties were not able to foresee when preparing the terms of the deal. Why the contracts need to be revised carefully, preferably combined with scenario analysis to try and foresee such unexpected events.

#### Vendor partnerships

Vendor partnerships is another sort of long-term contracts where the supplier and buyer work together closely. If the parties cooperate over time, the production efficiency and the quality of the products can often be increased. Something that can benefit the actors in the value chain in the long-run. The strategy has been successfully implemented by major Japanese car manufacturers, such as Toyota and Nissan, that have many long term partnerships with specialized suppliers (Johnson, et al., 2008). The partnerships may very well be determined by long term trust and collaboration, instead of specific long-term contracts. By working together, the companies can co-develop products and processes (Barney & Hesterly, 2015). Which may enable them to reduce cost and lead times, or to improve the product's specifications.

#### Franchising

Franchising is another type of common partnership, successfully implemented by many retail and fast-food companies. Franchising means that the parent company work closely together with their distributors, granting them benefits supplied by the corporate group. Where some of the most common benefits include marketing, sourcing and logistical support. One of the great benefit from franchising, rather than owning the stores yourself, is that much of the risk associated with running a store (Barney, 2011), is managed by an entrepreneur. This further grants the franchise-taker personal ownership of the business, thereby granting strong incentives to succeed with his or her business. The strategy has proven to be very successful in the fast-

food and convince store industries, implemented by actors such as McDonalds, Seven-Eleven and ICA. The companies are large groups benefiting from economies of scale in production, IT and logistics. That at the same time rely on the strengths of individual entrepreneurs when distributing and selling the goods. For the group, the strategy also reduces the bound capital in stores, and can greatly hasten expansion, compared to starting and developing the same amount of distributors organically (Johnson, et al., 2008).

#### 3.6.1.4 Mergers and Acquisitions (M&A)

Mergers and Acquisitions have been increasingly popular for most types of companies, where both investors and industrial actors are increasingly engaging in M&A activities. M&A can be seen as the main business model of an investment company, though can also be implemented further when developing a portfolio company. The portfolio company can be developed through adding on new segments through add-on acquisitions, or by merging it with another company. The strategy can be highly efficient when obtaining growth, where new customers and business segments can quickly be acquired (Johnson, et al., 2008). Therefore, the strategy is often implemented by investors quickly seeking to grow the revenue of a company.

A company should engage in M&A if the cost of acquiring the studied capabilities is lower than if they were to be developed in-house (Johnson, et al., 2008). M&A can be especially beneficial when seeking to strengthen the company quickly, since organic growth often takes time and requires large amounts of resources from the rest of the organization. However, implementing an M&A strategy can be cumbersome, and there often arises problems when integrating an acquired firm. Many of these problems relate to the cultural and organizational structures of the different firms, aspects that may be hard to integrate. These factors are often considered the main reasons behind why as many as 60-90 % of the global M&A activities are claimed to be unsuccessful (Oral source/s, 2015-2016).

There are several different reasons why companies engage in M&A, where some of the most commonly discussed are listed below (Ireland, et al., 2009).

- ✓ Increased market Power
- ✓ Overcoming entry barriers
- ✓ Cost of new product development and increased speed to market
- ✓ Lower risk compared to developing new products
- ✓ Increased diversification

- ✓ Reshaping the firm's competitive scope
- ✓ Learning and developing new capabilities

#### Increased market Power

The market power of a company can quickly be increased through acquiring competitors within the core market. The strategy is often implemented in mature markets or markets characterized by low growth, where it may be more profitable to acquire market share than it would be to capture it organically (Ireland, et al., 2009)

#### Overcoming entry barriers

Entry barriers is another important driver for M&A. Many Industries require large investments in infrastructure, such as production and distribution systems, that may be both costly, time consuming and hard to replicate (Barney & Hesterly, 2015)

. In those instances, M&A can be an effective way to gain entry to such markets, through the acquisition of an actor that had already developed such infrastructure. Another sort of entry barriers is regulatory hurdles, where an acquisition of a competitor already in possession of required legal documents could hasten the company's access to a market considerably (Ireland, et al., 2009).

#### Cost of new product development and increased speed to market

Developing new products is often risky and costly, and the firm may not have access to the competence needed for developing such products. In such an instance, M&A can be used to acquire start-ups or innovative companies to hasten their product development. In the high tech and life science industries, large corporations like Google and Astra Zeneca increasingly engage in M&A (Oral source/s, 2015-2016). Since it has often proven to be more profitable for them to acquire start-ups with new technology, than it would be to develop the technology themselves (Ireland, et al., 2009).

#### Increased Diversification and Scope

M&A can also be an effective way to increase the firm's diversification, as well as reshaping the scope of the company. By acquiring actors in new segments, the company can broaden its reach, thereby increasing its diversification and corporate reach (Ireland, et al., 2009).

Learning and developing new capabilities

The last driver for M&A is the access to new capabilities, competence and resources. Where such capabilities may be hard or even impossible to develop organically. Some practical examples of such capabilities include: patents, talent and systems or processes (Ireland, et al., 2009).

The different drivers for M&A, as well as the general characteristics of the strategy form a solid foundation for the analysis of an investment company, where both the investment company and its portfolio companies often engage in different sorts of M&A activities.

### 3.6.1.5 Resource Based View (the VRIO-framework)

The resource based view, or the resource based strategy model, is a model used to map and evaluate a company's resources and capabilities. This is done using the VRIO framework where the aim is to identify a company's key resources, and leverage those in order to capture competitive advantage. The meaning of the acronym VRIO will be presented further below. This model can efficiently be used when studying an investment company in order to understand the company's main capabilities and how they differ from their competitors'. The model is based on the definition that there are four different categories of resources and capabilities. These are *financial capital*, *physical capital*, *human capital* and *organizational capital* (Barney, 2011).

*Financial capital* includes all different sources of capital a firm can use to shape and implement new strategies. Some common sources of capital include: banks, investments from entrepreneurs or equity holders, and retained profits (Barney, 2011).

*Physical capital* relates to all equipment, machinery and technology available to the company. A category that includes any aspects effecting the equipment, such as geographic location of production facilities, retailers or distributions centers (Barney, 2011).

*Human capital* covers all of the people and human resources of an organization, a category including the know-how of individual workers, managers and entrepreneurs. It also covers supporting systems and routines developed for the people working there, including both tangible factors such as training programs and intangible factors such as professional relationships (Barney, 2011).

*Organizational capital* covers how the individuals in the organization are structured. The category includes all routines and processes upholding the organization, such as reporting systems and administration. The category also covers the intangible factors: culture, control systems, and the firm's reputation (Barney, 2011).

The resource based strategy model centers around four different questions regarding these resources and capabilities. These questions are:

1. Value – Do a firm's resources enable it to exploit an opportunity or eliminate a threat?
2. Rarity – Are these resources rare and only controlled by a few competing firms?
3. Imitability – Is it costly to obtain or develop the resources?
4. Organization – Is the firm's organization optimized to exploit its resources that are valuable, rare and hard to imitate?

If the answer is yes to all of those questions, then the firm is aligned to capture a competitive advantage. However, only a few firms are, and this framework can be used to identify these critical resources in order to and develop them further (Barney, 2011).

### 3.6.2 Business Strategy

The business strategy is the strategy set to guide each specific business unit of the corporation. The strategy should include: how customers are met, what products are to be sold, to whom, and what business opportunities are to be acted upon. A business unit may be a specific product, brand or market within a company and is generally defined in such a way that the firm can most effectively manage the different business. These are commonly grouped by similarity towards the customer or similarity regarding how the units are managed internally. The business strategy can be seen as an extension of the corporate strategy, determining what actual activities a business unit are to undertake, therefore its more precise and granular (Johnson, et al., 2008).

In this section, Porters generic strategies are first presented, which can be used as a tool to analyze a portfolio company's possible strategic choices. Thereafter Ansoff's product/market matrix is presented, a tool used for identifying new possible alternatives for growth. Another business strategy that is often covered in management theory, is the global or expansion strategy. The strategy mainly deals with expanding globally, however, such strategies should be considered obsolete for most larger corporations. For



larger corporations, going global is often not as much of an option, as it is a necessity, since it can allow the company to access new markets, suppliers and partners. Which allows the company to benefit from economics of scope and/or scale, greatly benefiting the company. However, some smaller local or regional actors can still successfully implement a more local strategy, where local benefits and niche markets may reduce the need for a global presence. Regardless, expanding globally should be an option evaluated by any firm, especially as a possible outcome when using the Ansoff's model. With that said, different geographical markets have different characteristics, needs and culture, aspects that needs to be revised carefully before pursuing opportunities in previously unknown markets (Johnson, et al., 2008).

### 3.6.2.1 Porter's generic strategies

According to Porter, the business strategy is centered around two main factors: cost and uniqueness, and the business unit should ideally develop a strategy based on either of the two categories. These two categories can be reached in different ways, which are described in the following matrix originally presented by Porter. The matrix includes the four main generic strategies: Cost leadership, Differentiation, Focused Cost Leadership and Focused differentiation. There is one additional fifth strategy, that some argue can work as an intermediary, or as “a best practice” strategy. Where some scholars instead claim that such strategies only cause companies to be perceived as stuck in the middle, with no clear focus. Each of these categories is presented separately below (Johnson, et al., 2008).

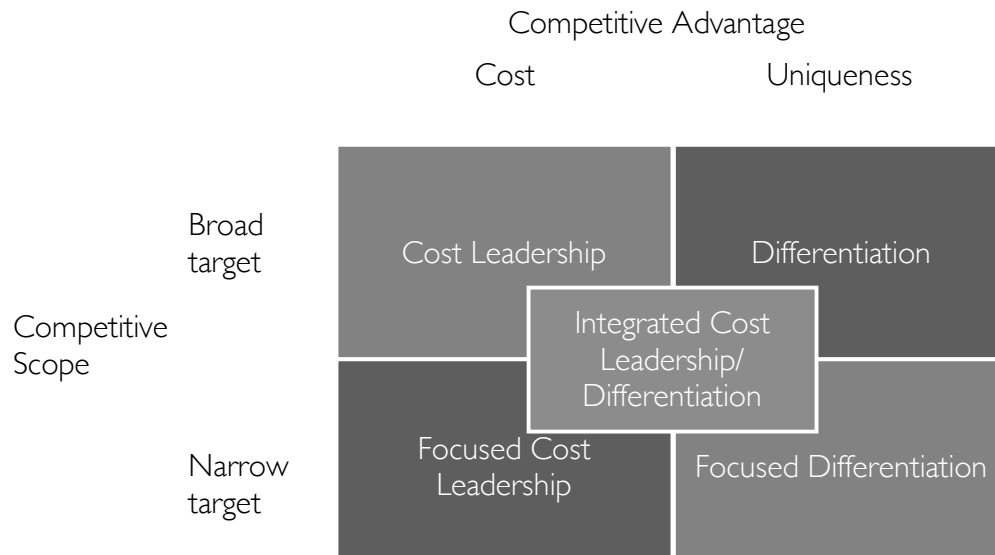


Figure 9: Porters generic strategies (Johnson, et al., 2008)

### Cost leadership

Cost leadership is a strategy aimed at offering the customers the lowest priced products or services on the market, beating the competitors through a lower price. This strategy is especially successful by companies offering standardized products or services in mature markets. The challenge of the strategy is to constantly cut cost to allow the company to reduce the price on the products and staying ahead of the competition, whilst at the same time ensuring a quality that is still acceptable by their customers. It can therefore be beneficial to cooperate closely with suppliers and distributors, in order to optimize the value chain. Companies only focusing on reducing price, no matter the consequence, risk ending up with a product or service that simply is not good enough (Barney, 2011). Where constant cost-cutting in combination with negligence could result in faulty products or bad processes, which could lead to accidents or negative public relations. However, when done right, the strategy may be extremely successful and can challenge existing industry standards. Evident in the airline industry, after the entrance of low cost alternatives such as Delta Airlines, Ryan Air and Norwegian (Johnson, et al., 2008).

### Differentiation

Instead of competing on price, a company can choose to develop and differentiate the product or service, competing through quality or uniqueness. Cost leaders typically target a general type of customer, through a broad and standardized offering. Where an actor implementing differentiation instead target a specific type of customer or niche segment. The offering can be developed to best capture the needs of that segment, and be presented in a way that is best suited for the targeted customers. To succeed with such a strategy, it is important to truly understand the customer, their buying behavior, and what qualities or services they value (Barney, 2011). Furthermore, customers only favor the differentiated product if the perceived increased value exceeds the price premium. It is therefore crucial to understand not only what the customer wants, but what they are willing to pay for. Such factors include intangible aspects such as design and customer service, as well as more tangible differences such as quality and durability. Additionally, since the strategy focuses on specific customer segments and constantly outcompeting the competitors in that segment. It is necessary to continuously develop and enhance the product or service, to stay ahead of the competition (Johnson, et al., 2008).

Focus Strategies: Differentiation or Cost

Apart from the cost and diversification strategies, there is another type of strategy that firms can use to diversify. That is to combine the uniqueness of the offering, with a targeted market or customer segment. Such segments can include: a particular buyer group (such as elderly or kids), a specific sales channel, a professional segment (such as painters or professional gardeners) or a geographic market. The focus strategy varies from the differentiation strategy in the way that it selects a specific segment in which to compete. Where the differentiation strategy rather refers to how a company is to present its offering (Johnson, et al., 2008).

The focus strategy can be combined with both the cost leadership and diversification strategies, to further allow the firm to distinguish itself from its competitors (Barney, 2011). One firm that can be seen as a successful leader in a focused cost-leadership strategy is IKEA. IKEA have a clear cost leadership strategy which has gained them a considerable global market share. Furthermore, IKEA have combined the strategy with a focus on young families. Where services such as long opening hours, in store restaurants and a broad portfolio of family oriented products have gained them a strong position within the young family segment. One example of a focused differentiation strategy is build-a-bear, who have chosen to differentiate themselves from other distributors of stuffed animals. At their build-a-bear-workshops the customer does not only select and stuff the toys themselves, but also selects different sorts of accessories and outfits for the animal. A clear differentiated offering combined with the focus on the targeted group: kids and their parents (Johnson, et al., 2008).

Integrated strategies, "Stuck in the Middle"

A firm may complement their cost leadership or differentiation strategy with secondary activities to attract a broader set of customers. This is often hard to achieve since the firm risk being interpreted as un-focused, thereby becoming less attractive than focused competitors. The firms that have successfully implemented such strategies often have a clear focus that they support with very specific activities that are often time limited (Barney, 2011). One example of such a firm include Target, that complement their cost-leadership strategy with partnerships with notable designers in make-up and fashion. Another example is HM, who also have a clear cost leadership strategy that they during limited time periods have successfully complemented with premium fashion designers. Since it is such a risky strategy, a firm should only pursue it if it has already established a clear and strong position in its core market (Johnson, et al., 2008).

### 3.6.2.2 The Ansoff Matrix

The Ansoff Matrix provides an efficient tool for mapping and evaluating potential growth strategies for an organization. The company can either continue on its current path, strengthening their position in existing markets and products, or develop new markets or products (Ansoff, 1957). One important aspect to note about the model is that it only covers growth, which is not always transferred into profit or value. Therefore, the mapping should only be used as one of several steps when evaluating new initiatives. Where further analysis is required in areas such as profitability, strategic fit and potential risks of the initiative (Johnson, et al., 2008).

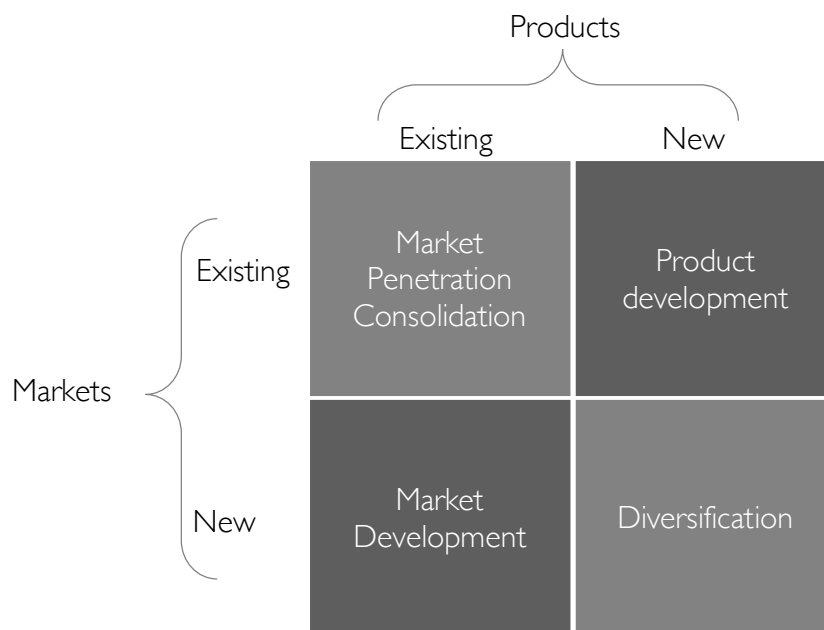


Figure 10: The Ansoff matrix (Ansoff, 1957)

An organization generally starts in the top left square of the matrix, with an existing product or service in an existing market. If the organization seeks to grow, it must do so either by staying in that square, further penetrating the market, or by developing new areas of the matrix. If the organization have a strong offering expected to be well received in a new market, a marketing development strategy may be fruitful, where new markets are entered (Johnson, et al., 2008). If the company instead have developed strong sales channels and have a strong market presence, a widened product offering may be the best alternative. The final area of the matrix: diversification, means developing a new product or service offering, to be offered in new markets. The diversification strategy may sound bold, though is implemented in many

conglomerates or investment companies when developing entirely new companies or business units (Johnson, et al., 2008).

The product development strategy does in general require the organization to develop new technologies and processes. Where investing in such capabilities may involve substantial risk that need to be accounted for. The benefit of this strategy is that it can be built on existing customer knowledge from the current markets, which may facilitate the product expansion (Johnson, et al., 2008).

The market development strategy does not only include the development of a new geographical market, but can also cover the development of new users or segments. In that case, a new target group or type of user is included in the offering. These groups can be found through analyzing consumer pattern, or new potential user categories that are new to the product. It is highly necessary to tailor the offering for the new market, where differences in consumer patterns, culture or needs could result in very different requirements from the customers (Johnson, et al., 2008).

### 3.6.3 Functional Strategy

The functional strategy focuses around translating the business strategy into specific goals for each different function or departments in the business unit. Therefore, the functional strategy concerns how the business strategy is to be achieved in practice. A functional strategy is typically set for each different department or function, where some examples of such functions include: human resources, finance and production. Some factors that are often included in the goals that are set include: what resources to use, how processes are to be shaped, and how people are to prioritize their work. Where the overall goal is to ensure that the operational part of the business is structured to best utilize the firm's key resources and capabilities. Furthermore, the outcome of the business and corporate strategy is completely dependent on the work done by the different functions of the company. Hence, the functional strategy should be seen as critical when creating the underlying value of the company. The strategy must therefore be well communicated, so that all units know how to achieve success towards the overall strategy (Johnson, et al., 2008).

From an investors point of view, the functional strategy is targeted by some, but not all investors when developing a portfolio company. There is often a great distinction between industrial and financial investors. The first category often seeks to leverage industrial experience when tackling functional

development. Financial investors however often mainly develop their companies on a corporate and business level (PWC, 2015). Why the studied investors involvement in the functional strategy may vary. Nevertheless, financial investors sometimes use industrial advisors and consultants to develop the functional strategy of a company. Why it can be hard to separate the two based on what parts of the organization they develop (Oral source/s, 2015-2016).

This rest of this section is categorized using the different steps of the value chain model presented by Michael E. Porter. The value chain can be found in the following illustration and consists of different sets of activities and functions. Each activity will be presented thoroughly, as well as some tools and strategies for each category. Note that the different logistic activities are grouped together, and presented together with operations, due to the strong linkages between the activities (Johnson, et al., 2008).

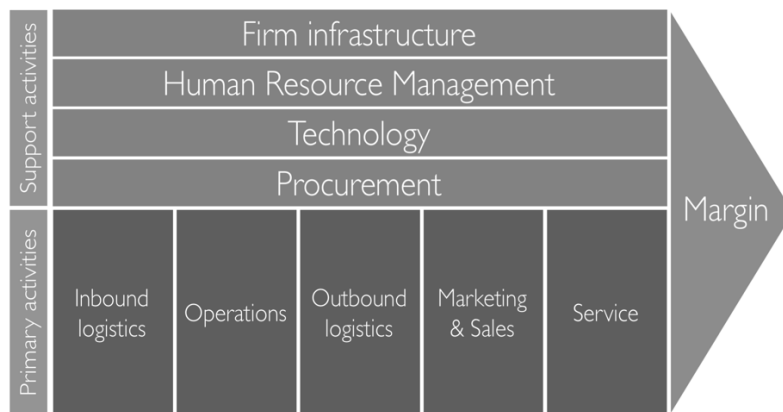


Figure 11: Porter's Value chain (Johnson, et al., 2008)

### 3.6.3.1 Firm Infrastructure & Organization

The support activity firm infrastructure include all supportive functions tasked with assisting the company with its daily operations. The most basic necessities for a company are included in this activity, such as accounting, legal affairs, administration, structure and management of the company (Johnson, et al., 2008).

Some of these activities are non-essential when discussing company development and value creation. However, there are some activities included in the infrastructure function that can be developed to increase the company's value. Some of the most common ones include the functions: finance, legal,

tax and external communication. The finance function can for example reduce the financial costs of the company, and ensure that the company has access to cheap debt. Additionally, the legal and accounting functions have a critical job when ensuring IP-rights and reducing tax-spend. Furthermore, the communications department can identify and regulatory changes or manage external communications during a crisis. These are just some examples of how an efficient infrastructure can help the company capture value, why these support activities should be monitored when analyzing a company (Oral source/s, 2015-2016).

### 3.6.3.2 Human resource management

The support activity human resource management (HRM) covers the activities related to managing the staff of an organization in the best way possible. The main activities included in HRM are: staffing, workplace policies, benefits and compensation, retention, training, handling employment laws, and employee protection. Many of these factors, such as attracting, retaining and developing talented individuals, are crucial when forming a well-performing company (Dias, 2016).

Apart from the pure tangible factors of HRM mentioned above, the function is tasked with creating a positive work-environment in which people will want to work. This includes managing the culture of the company, which is often accredited for being one of the main issues when developing a newly merged or acquired company. Hence, the HR-function needs to be analyzed both in terms of how they are handling their main tasks, as well as the intangible factors that help shape the culture of the company (Isaksson, 2006).

### 3.6.3.3 Technological Development

Technological development can be defined as the way a firm handle: equipment, hardware, software, processes and know-how, when refining input resources into products. The broad definition includes all surrounding aspects when managing technology, such as the development of new technologies, optimization of processes and innovation management. A company's dependence on technology depend a lot on its industry. Why the industry dynamics needs to be assessed before reshaping the RnD activities. This underlying industry understanding is optimally used when defining the goals for the company's technological advancements, as well as allocating required resources to the RnD-department (Isaksson, 2006).

Developing a company in a fast moving industry requires other sorts of skills and tools than for a company in an industry changing at a slower pace. Some

activities that can be crucial in a fast moving industry include: the handling of intellectual property rights, the management and prioritization of the RnD department, and how focus is shifted from legacy products to new development. Nevertheless, the pace of innovation has increased across all industries. Why changes to the industry or market must be constantly monitored, since a technological shift could have a significant impact on the company and its markets (Dagens Industri, 2015).

#### 3.6.3.4 Procurement

The procurement function is responsible for all of the activities that are associated with the acquisition of input material from a supplier. This includes the two main tasks sourcing and purchasing. Sourcing means finding, selecting and managing the supplies needed for running the company. Thereby including key task such as determining: what relationship the company is to have with its suppliers, the assessment of suppliers, and how the company is to prioritize between cost, reliability and deliverability. Purchasing concerns how resources are best acquired, focusing on what methods, routines and experience are used when reaching a purchasing decision. Some of the key tasks of the purchasing activity include: investigating the technical or functional needs of a resource, the total cost of ownership, how the purchase is to be financed and the selection of the most suitable payment method (Weele, 2014).

In general, 50-85 % of the total cost of goods sold in a manufacturing industrial company comes from the products or materials that are purchased from its suppliers. Therefore, the function can be critical when developing the company, since relatively small improvements can have a great impact on its profitability. Furthermore, the sourcing task can have should also be considered essential, since bottlenecks in supply can lead to grave consequences to the operational efficiency of the company. Hence, the selection of the right suppliers and sourcing practices can be crucial, when both managing cost and the operational stability of the company (Weele, 2014).

#### 3.6.3.5 Logistics and Operations

The first three primary activities in the value chain are related to how input and output material are transported and refined. The main goals of these activities is to manufacture and deliver the products offered in the best possible way. These activities include the inbound and outbound logistics of the firm, as well as the operations or manufacturing. One of the main goals for these activities is to reduce the total cost, whilst at the same time ensuring



the quality and deliverability of the products (Jonsson & Mattsson, 2011). Due to the activities' strong impact on the profitability of the company, the function has grown in importance, especially for an investor developing the profitability of the company. In industrial companies, the operations activities often amount for 50-80 % of the entire cost base, and the freight cost between 10-30 % (Jonsson & Mattsson, 2011). Why optimizing intermediary storages, supply levels and transportation methods can have great effects on the performance and value of the company (Weele, 2014).

#### 3.6.3.6 Marketing & Sales

The fourth primary activity of the value chain is the activity marketing and sales, which is tasked with selling the products or services offered by the company. Some key functional strategies and activities performed by the department include: pricing strategies, sales-channel management, marketing and promotion activities, and brand management. These activities can be studied using the 4-P model, which is a generic grouping consisting of four categories: Product, Price, Placement and Promotion. A model that is designed to help the user to map and determine how these four core activities are to be organized (Armstrong, et al., 2009). Since the marketing and sales activities are crucial for driving the sales growth of a company, they are often targeted by investors when developing the growth of a company (Oral source/s, 2015-2016).

#### 3.6.3.7 Service

The fifth and final primary activity of the value chain is service. The activity covers all actions that are connected with the service offering made by the company such as: repairs, spare parts, warranties, guarantees installations, updates, training or other activities increasing the value of the product (Johnson, et al., 2008). Service is most often offered to increasing revenue, to enhance a customer's experience of a product, or a combination of the two. Service agreements can be very profitable why they are frequently used by a variety of companies. They can also prove to be a competitive advantage, especially in industries that are in need of frequent or fast repairs. This is the case for many larger manufacturing plants, where production stops can be extremely costly. In such a case, access to fast service can be vital for the production and profitability of the plant, why the service of faulty parts can be essential (Oral source/s, 2015-2016).

## 3.7 The Investor's Perspective

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In the section *Levels of Strategy*, different methods and strategies were presented, that can be implemented when developing a portfolio company. However, these models focus on the development of a particular portfolio company, why the investor's perspective needs to be added. The following sections are aimed at granting an understanding of the characteristics of the investor, which will be used to give a better understanding of the interactions between the investor and the portfolio company. The section will first cover the topic: investment strategy, which grants an overall understanding of how that strategy can influence the development of a company. Thereafter, change management, agency theory and incentive programs will be presented, due to their central role in the development of a company.

### 3.7.1 Investment strategy

The investment strategy determines the overall scope of the investment company, determining what companies the investor is to invest in. Hence, it is used as a guideline when discovering new prospective investments and determining how current and future companies are to be developed. The investment strategy usually includes the areas: investment horizon, expected return on investment, what dividends shareholders can expect, development practices and what industries or geographical markets are targeted (Oral source/s, 2015-2016).

Many of the larger Swedish private equity funds tend to have an ownership horizon of 3-7 years, and act within a set number of geographical markets, such as Sweden, the Nordics or western Europe. Other investors, especially private ones, tend to favor longer ownership periods (Oral source/s, 2015-2016). Historically neither of the two groups have tended to focus on one single industry. Instead they investigate a broader range of prospects in the hopes of finding the most profitable alternative. However, today there are many exceptions where niche actors target a certain industry, where industries such as digital, fin-tech, telecom or life sciences have become increasingly popular among investors. These actors are growing in number, and the increased competition in the industry is forcing investors to find new ways of distinguishing themselves (Dagens Industri, 2015).

Some examples of investment strategies are presented below, for some of Sweden's most well-known PE-investors. Note that these strategies are greatly simplified in order to grant an overview of the industry, rather than an in-depth understanding for each company.

<p>Segulah            Type of investor: Large PE-funds            Industries: Broad range of industries &amp; sectors            Geography: The Nordics            Hold period: 5-7 years</p>	<p>Ratos            Type of investor: Evergreen PE-investor            Industries: Broad range of industries &amp; sectors            Geography: The Nordics            Hold period: 3-14 years</p>
<p>Lifco            Type of investor: Evergreen PE-investor            Industries: Broad range of industries &amp; sectors            Geography: Global, focus: European companies            Hold period: long-term / indefinite</p>	<p>Nordic Capital            Type of investor: Large PE-funds            Industries: Broad range of industries &amp; sectors            Geography: The Nordics            Hold period: 3-7 years, average 4,6 years</p>

Figure 12: Investment strategies for selected investors, information gained from the companies' webpages (retrieved spring 2016)

## 3.7.2 Change Management

Change management as a topic covers how overall change can be lead and initiated, which in length includes how companies can be developed and transformed. This topic will only be covered briefly due to the limitations of this report, why two of the more commonly cited works on change management are presented. The first one is John P. Kotter's 8-step model on change, as presented in his book *Leading Change*. The second author is Jim Collins, whom in his work *Good to Great*, presents the results of his 5-year study on successfully transformed companies. Thereafter, a change management process by McKinsey & Company is presented, a process that aims to grant a fundamental understanding of how business development can studied as a process.

### 3.7.2.1 Kotter's 8-step model

According to Kotter, the first steps of a successful transformation Is to create a climate for change. This should be done through three activities: enforcing a sense of urgency in the organization (1), forming a coalition leading the change (2), and developing a vision and strategy for the organization (3). Thereafter the whole organization needs to be engaged and enabled, which should be done through the steps: communicate the vision (4), empower

action (5), and getting quick wins (6). In the final phase of the program the change needs to be implemented and sustained. Which is to be done through: leveraging wins to drive change (7), and by embedding the change into the corporate culture (8) (Kotter, 2007).

These steps grant a deeper understanding of how different actions may be shaped when transforming a company, why they will be used as a baseline when investigating the actions made in the studied companies. Furthermore, it illustrates a number of areas that Kotter has determined to be of great importance when transforming a company. Areas that will be used when comparing the empirical data to the theoretical data (Kotter, 2007).

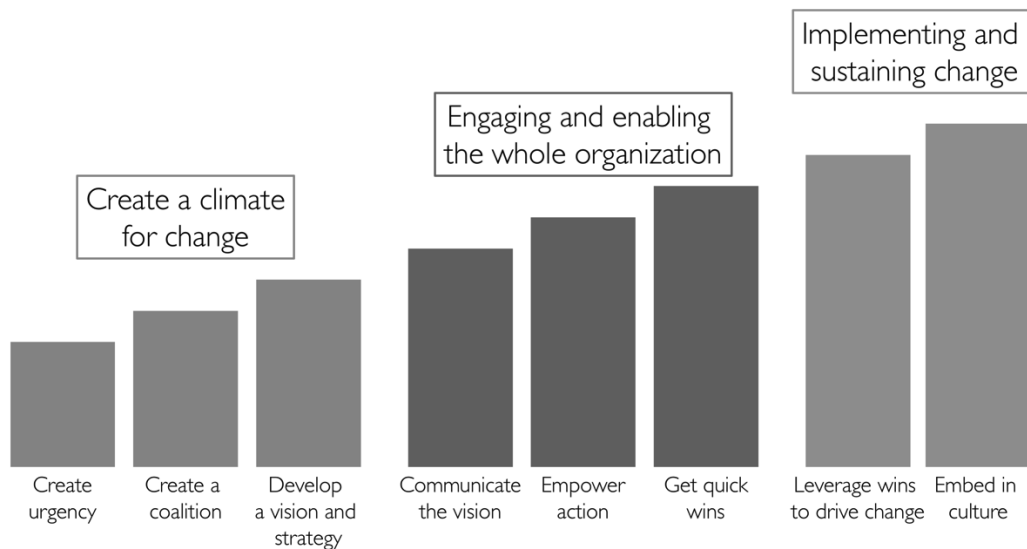


Figure 13: Kotter's 8-step model (Kotter, 2007)

### 3.7.2.2 Jim Collin's Good to Great

According to Jim Collins, one of the keys to successfully transforming a company is to establish a strong management team. Which is to be done by finding the right people and getting rid of the ones that are hindering change, as fast as possible. Hence, the transformation will most likely only be successful after having formed the right team, with the right people in place. Something he explains as simply as: “first who, then what”, which illustrates his determination that the management team is one of the most critical aspects in the early stages of development. He claims that such teams ideally consist of a set of determined team players. Where their previous experiences and track record are not as important as a humble approach and a willingness to inspire and connect with the people around them. It is far more important for these people to ask the right questions than always being able to give the right answers (Collins, 2003).

Collins discovered that leaders with the personally trait determination where much more likely to succeed long-term, which illustrates the importance of having the right leaders with the right personality traits. Leaders that instead implement a more status-oriented leadership style could be successful in the short term. However, he claims that they seldom manage to develop the people around them, resulting in an organization depending on a central leader (Collins, 2003). An organization that is often less resolute, and risk falling apart in the absence of the central leader. Thereafter he points out the importance of creating a strong disciplined culture, guided by strong clear messages, much according to the communication-steps in Kotter's model.

There are similarities between the two authors work, when comparing Kotter's model's steps, to some of Jim Collins key insights. One of the most critical ones is the fact that both authors point towards the benefits of a strong leader and management team, where both agree that a strong team or coalition is needed. It is therefore important to study how the change and transformational development is managed in the studied companies.

### 3.7.2.3 The Change Management Process

The transformation or development of a company is often done in different steps that are often translated into a development process when discussed by the industry and academia. The steps of this process is often similar regardless of the studied company, however, the content of each step will likely differ greatly when comparing companies from different industries. To grant an overall understanding of how change management can be seen as a process,

the following process model is presented. This particular model was presented by the strategy consultant firm McKinsey & Company. There are several other models similar to the one presented, where some differed slightly when examining the subsections of each step. Regardless, the overall idea of the process was the same in the different models, which supports the idea that business development can be studied as a process. This particular model was selected due to McKinsey and Company's strong standing in the industry, since the company it is considered to be one of the highest ranking strategy firms globally (Bradley, et al., 2012).

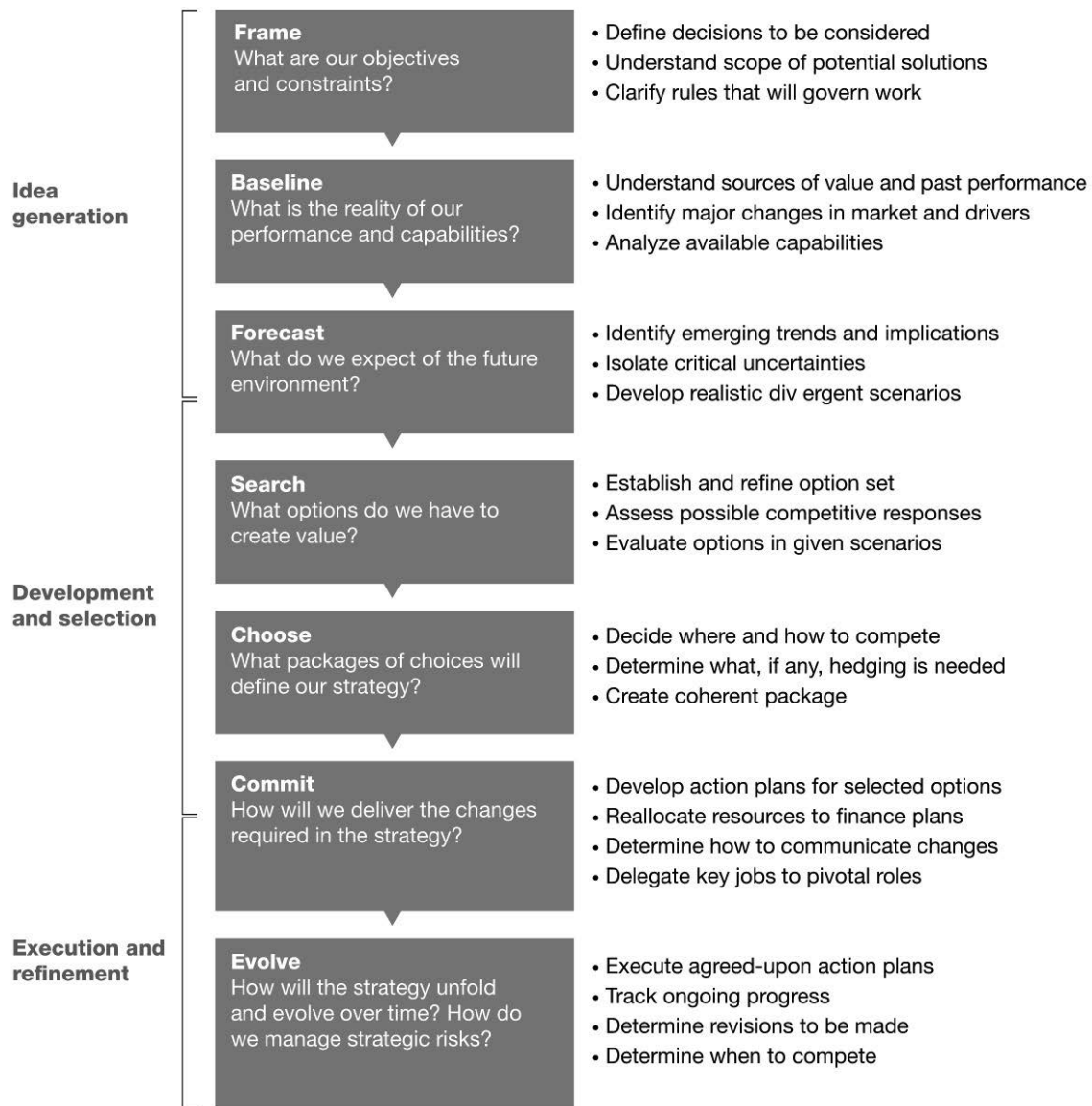


Figure 14: The development process (Bradley, et al., 2012)

### 3.7.3 Agency Theory & Incentive programs

Investors frequently use incentive programs to motivate, retain, attract and align their employees. These use of incentive programs have grown at a fast pace during recent years. Which can be illustrated by the fact that the equity-based share of the total compensation for senior managers in American corporations grew from 20 % in 1990, to 70 % in 2007 (PWC, 2011). There is less data available for Europe and Sweden, though the trend can be seen in Sweden as well. Where both privately owned and commercial PE actors often grant their portfolio companies' CEOs large stock-ownership and stock-options programs (Strandberg, 2015) (Hägerstrand, 2015). Due to their frequent use, it is important to analyze and investigate how these programs are formed by the studied investor.

#### Agency Theory

The core concept of agency theory is the agent principle problem, a problem that arises when two parties enter a binding contract where one of the parties, the so called agent, can act on behalf of the other party. The problem is caused by the agent's inclination to act in a way that is primarily beneficial for the agent, by acting on self-interest or to avoid personal risk. This situation occurs daily in the workplace, where a normal employment contract is an example of such a situation. This situation can become especially problematic at senior management level, due to the increase of the agent's levels of control and influence. One example of when this issue can lead to negative consequences for the firm is the following: a CEO decides to lead the company through a safe and risk-averse strategy, despite it being objectively less favorable for the shareholders. Such a situation could be caused by acts of self-interest, where the agent may want to ensure his or her continued employment, something a more "safe approach" would ensure. Another example is if the CEO shape the company to reap personal short-term benefits, at the expense of superior long term profits. This can occur when a manager work fraudulently to secure an upcoming yearly bonus. These are just two examples of how the agency problem can cause issues for the organization and its owners, why it should ideally be addressed by the owner of the company (Eisenhardt, 1989).

One way to eliminate or minimize the agent-principle problem is to align the interests of the agent and the principle through economic incentives. If the CEO in the previous example where to own a significant stake of the company, he or she would be incentivized to choose the option that benefits the company the most. The shareholders can implement such incentives to ensure that the interest of the managers and employees are aligned with their

own. However, the programs can potentially backfire, where the programs could favor the agent to act on self-interest or avoid risks. One example of such a scenario would be an employee choosing a less risky investment, due to the employee's strong dependence on the incentive programs. The riskier investment could be turned down despite it being objectively superior, if the risks of the investments supersedes the employees risk appetite. This can be caused by situations where the employee has a large stake of his or her own financial assets allocated in the incentive programs. A situation that would be worsened if the agent were to leverage themselves by funding the incentive programs through loans. The rest of the shareholders may likely have a more diversified portfolio, often leading to a higher acceptance of risk, which would favor the riskier but more profitable option. Since such a situation would counteract the alignment of the two parties, it is important designed the programs with factors such as leverage and risk appetite in mind (Eisenhardt, 1989).

#### Types of Incentive Programs

Incentive programs can be shaped in a lot of different ways and often differ depending on the seniority of the employee that the program is intended for. In general, the programs are designed to reward the employee for their performance and to align the interests of the employee with that of the company and its shareholders. Since investors primarily deal with top executives at CXO-level, only the most common ones designed for such executives are covered in this study. These incentives are: bonuses, stock-ownership and stock-option programs (PWC, 2015). A lot of varieties of the three exist, though only the most basic designs of the programs are described in this study (Grant Thornton, B, 2015).

Bonuses are the simplest incentive, meaning that a reward, often monetary, is granted when an employee reaches a certain goal. These goals should be designed to best reflect the desired performance of the employee, so that he or she is incentivized to work efficiently. However, such goals can be hard to distinguish for C-suite executives, since their duties are often very broad and intangible. Therefore, company related performance metrics are often used, such as turnover, growth or profit (Grant Thornton, B, 2015).

Stock ownership means that the employee buys, or is given a set of stock, thereby becoming a shareholder. The incentive reward the employee through the potential increase of the share's market value, as well as getting access to any potential dividends. However, if the stock value decreases, so does the



value of the incentive, where an employee can even be “punished” in the event of a downturn (Grant Thornton, B, 2015).

Stock-option programs are designed so that the employee is allowed to buy a set amount of future stock, at a price equal to the current market value of the stock. That means that the employee is not bound to buy the stock at the event of a decrease in the share’s value, thereby reducing the negative impact of a downturn in the stock’s value (Grant Thornton, B, 2015). These programs can either be granted for free, or priced at the market value, which influences the value of the incentive. In Sweden a fair market-price according to the “Black and Scholes formula” is often used, due to tax-related costs and administration (Oral source/s, 2015-2016).

There are several drawbacks associated with the different incentive programs. For the stock-related programs the incentive can be heavily influenced by the volatility of the stock market, despite the employee’s lack of influence on it. Hence, the value of the incentive is partially defined by market fluctuations rather than performance, undermining the incentive’s ability to motivate through a pay-for-performance structure (Grant Thornton, B, 2015). Others claim that the linkage between pay and performance is minor at best, why it is important to note that not everyone agree that incentive programs are optimal when trying to motivate employees (Herzberg, 1987) (Desai, 2012) (Jensen & Murphy, 1990).

### 3.8 Theory Summary

The theory section in this study aims to form a strong foundation for the analysis of a private active investor. The introduction to this section, with its description of corporate governance and the board of directors, combined with the section *the investor's perspective* forms the basis needed for understanding the investor that is to be studied. These two sections should grant an understanding of the characteristics of the investor and how that might influence the investor's development of a portfolio company. Thereafter, the model *three levels of strategy* is used to structure the strategic options available to a company, where different tools and strategic options are presented for each level.

These different sections have been merged to form the holistic model presented below, representing an investors options when developing a company. This model should be considered a linear process, initiated through the acquisition of the portfolio company. Where the development process presented by McKinsey & Company will be used to grant an initial generic structure for this process. After the first initial transformation, the process should be seen as cyclical, since the following development, after the initial transformation, should be seen as continuous rather than linear.

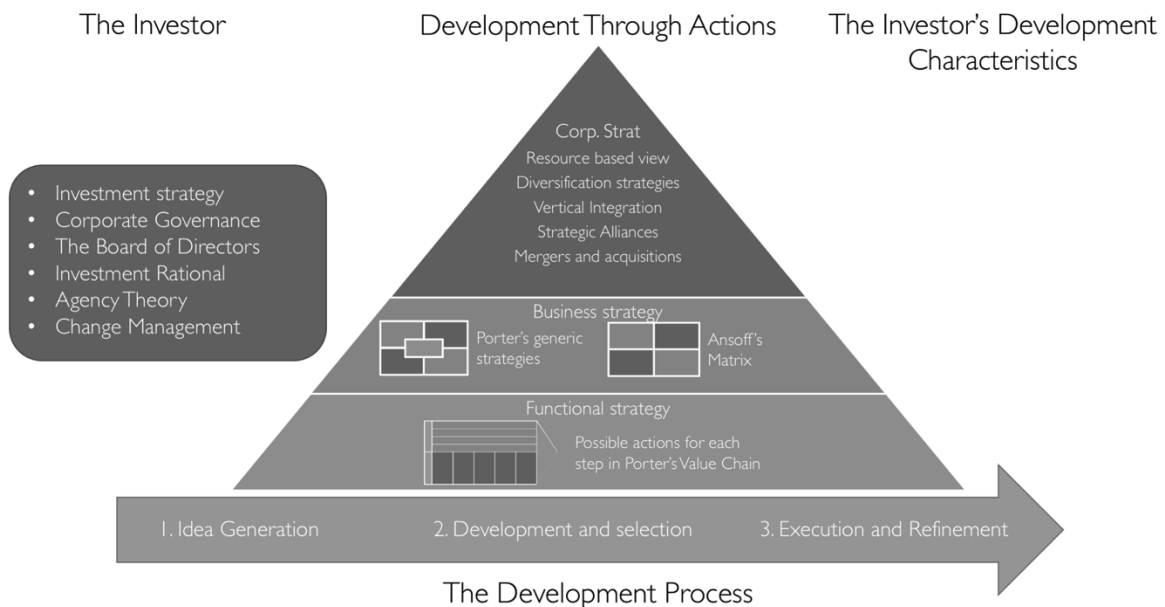


Figure 15: Framework for analyzing investors

When examining the available publications, it is clear that there exists a gap when studying private active investors. Most studies focusing on private equity tend to focus on financial investors and commercial PE funds. The models presented mainly focus on the administrative aspects of an owner's or investor's interactions with a portfolio company. Why such models tend to focus on financial reporting and responsibilities between the investor and the portfolio company. One of the reasons for the lack of in depth studies on private investors and the development made, is due to the sensitive nature of the material needed. Most owners and investors do not feel confident sharing critical information regarding their portfolio companies or their investment practice. The following model was designed to help bridge the research gap, as presented in the problem statement, that exists due to the lack of sufficient models on this type of business development. Furthermore, the study's focus on private investors is due to the lack of studies within that area.

The focus of this study, will be on the actions made when developing newly acquired companies. Therefore, the models presented in this theory section will grant an understanding of the investor, and the actions made in the portfolio companies at corporate, business and functional level. When studying the empirical data, the information gained will be categorized in order to identify similarities and differences in how the companies have been developed. This information will be used to try and answer what strategic levels of a portfolio company the specific investor seeks to develop, and through what activities. Information that can potentially be used by another party when comparing or measuring other investors.

## 4 EMPIRICAL STUDY

During the empirical study, one investment company and four of its portfolio companies were studied. This section will first briefly present the investment company, which is then followed by a brief introduction to each of the four portfolio companies. Furthermore, additional information is presented regarding the interviewees and their roles in the different companies. Thereafter each portfolio company is presented, where the focus of the text is to reveal the most critical events and activities initiated in each company.

The information presented about the portfolio companies is divided into three different parts. The first part covers the first three to six months after the acquisition. The part section covers the following time up to one and a half year after the acquisition. The final part covers any notable events that have happened thereafter and up until five years after the acquisition. Ultimately, the information is summarized in a table, with the purpose of granting an overview of the actions made.

### 4.1 The Investment company

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The investment company studied in this thesis is a private family controlled investment company. It currently owns a large number of varied companies, and tend to favor investments in the range of 50-1 000 MSEK. The company does not favor any specific industries, though tend to avoid investments in fast moving high tech and bio tech industries. The company primarily invests in companies in the Nordics with local, regional or global sales.

The company consists of a number of senior business developers, with strong industrial backgrounds. Most, if not all of them, have successfully lead Nordic medium and large sized companies, both private and listed ones. Furthermore, they develop their portfolio companies through active ownership, by expanding the board to include senior business developers and external experts. Thereafter, the companies are developed through the CEO and through the board. Where the boards have close co-operations with the portfolio companies when developing both the corporate, business and functional strategy of the company. They use the industrial experience from their business developers and board members to support the portfolio companies' senior management when developing the strategic and operational aspects of the companies. The companies are monitored on different levels, which generally include: a close cooperation between the

CEO and the chairman of the board, weekly connections between the company and the investors, monthly reports and extensive analysis before each board meeting. Four ordinary board meetings are generally held each year per company, followed by additional meetings when deemed necessary.

The investors strongly believe in incentive programs, particularly standardized share-ownership programs, where more complex or option-based programs are avoided. Their programs are designed to create a sense of pay-for-performance, where tangible results are rewarded. The remuneration for senior managers are held at moderate levels when compared to the industry average, combined with substantial share-ownership programs. According to the investors, the goal is to grant sufficient pay, where the managers' pay and rewards are to be aligned with the investors' interests. This practice includes external board members and business partners, whom are generally asked to partake in share-ownership programs.

#### 4.1.1 Large.Corp

Large.Corp is an industrial manufacturing company offering safety-related premium components to a global niche market. Their product is in many ways superior to that of their competitors, and produced at lower costs due to highly efficient operations and manufacturing practices. It has been held by the investment company for several years and has shown strong growth in turnover and profitability throughout the years, exceeding that of their industry peers. One of the main drivers for their success has been a combined organic and inorganic expansion model, acquiring key distributors and expanding own sales offices. The company has successfully developed their patents to ensure the longevity of their competitiveness, as well as improving industrial processes, lowering cost, increasing productivity and managing risk. Since the acquisition, the company's turnover has been increased by 300-400 %.

#### 4.1.2 Auto.Corp

Auto.Corp is an industrial manufacturing company serving the automotive industry, supplying niche products. It has undergone great change during its limited ownership period where the organization and its practices are being developed to allow for acquisition-based growth. The main objective of the current transformation is to prepare the company for an aggressive expansion, through a set of future acquisitions meant to increase their product portfolio. The company is yet to prove itself though show promises through improvements to their structure and organization.

### 4.1.3 Chem.Corp

Chem.Corp manufactures and distributes chemical products and handle waste products from neighboring industries. The company was founded by the investment company some 12-16 years ago. Since then, the company has been successfully grown into a dominant actor within its field through series of acquisitions. Furthermore, they have continuously developed their operations and supply chain. Which has allowed them to reach a profitability that is unmatched by their competitors.

### 4.1.4 Constr.Corp

Constr.Corp is an industrial manufacturing company within the construction sector, supplying niche products to the larger Swedish construction companies. The goal of the investment is to expand aggressively and the company has already established new offices throughout the Nordics. However, the company has faced management issues, where key managers have been replaced. Despite these issues, the company show increases in sales and profits, where the current development is expected by the board to lead to continued improvements.

## 4.2 Key interviewees and board minutes

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The business cases are based on interviews with senior managers, board members and investors, as well as board minutes from the studied period. The focus of the study has been on the first five years (when applicable) after the acquisition. The key interviewees that have been interviewed in this study are presented in the following matrix, to illustrate their involvement in the different portfolio companies.

The positions shown in the following matrix represents a position that they have held during any time during the researched period, which explains why some of the positions may appear to overlap. For each company the chairman of the board, and board members have been interviewed. Furthermore, CEOs and senior managers were interviewed at Auto.Corp and Large.Corp.

The people interviewed have experiences from leading or investing in Nordic companies, where many of the interviewees have close ties to the investment company. Many of the interviewees have vast experiences from successfully leading large Nordic industrial companies. Some of the current or previous experiences of the interviewees include: being the CEO and/or chairman of the board for Large Cap Stockholm listed companies, and being a member of the board and/or senior manager at large privately controlled companies. The goal of the interviews has been to gather information from both investors, external board members and senior managers, which explains the roles of the interviewees. External board members have been interviewed in some, but not all of the cases, due to the fact that not all of the companies' boards' have external board members.

It should be noted that if nothing else is stated, all of the information presented in this section has been gained from the interviews, board minutes or observations. If so, no additional notation will be presented.

	Auto.Corp	Constr.Corp	Large.Corp	Chem.Corp
Interviewee 1			B	ChB
Interviewee 2	B	ChB	ChB	
Interviewee 3	B		ChB	
Interviewee 4	ChB		CEO	
Interviewee 5		B	M	B
Interviewee 6	B	B		
Interviewee 7	CEO			
Interviewee 8			B	B
Interviewee 9	M			

Figure 16: Key interviewees

ChB	Chairman of the board
B	Board member
CEO	Chief executive officer
M	Senior management position



## 4.3 Large.Corp

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Large.Corp has undergone great changes since the acquisition by the investment company, some 8-12 years ago, resulting in high increases in turnover and profit margin greatly exceeding the industry average. Some of the most important activities made by the company at senior level, will be presented in this section. These are divided into three different parts: the first part covers the first year, the second part covers the second and third year, and the final part presents some notable events that occurred thereafter.

Key Figures for the Company	
Industrial manufacturing company	
Industry:	Construction
Turnover:	1 500 – 2 000 MSEK
Growth last 5 years:	40 % CAGR
Employees:	500 – 700
Avg EBITDA:	20-25 %
Reach:	Global sales
In portfolio:	8 – 12 years

Figure 17: Key Figures for Large.Corp

### 4.3.1 Part One: Supporting a Strong Organization Forward

#### The Company and the Business Case

Before the investment company's entry, Large.Corp had been led by the entrepreneur whom had founded the company. One to two years prior to the acquisition, he decided that he wanted to sell the company and therefore started to ready it for a change in ownership. The entrepreneur was both the majority shareholder and the CEO, something that he set out to change as a part of the preparations. A new external Chairman of the board was recruited, as well as a new marketing and sales director, whom were to take over as the CEO after having learnt about the company. Together they prepared the organization for a change in ownership, where the new external managers were tasked with the development of the structure and stability of the company.

The investment company acquired the company about a year after the organizational change. By then the new CEO and chairman of the board had

made significant changes to the structure of the company. New routines and work processes had been set in place, which increased the stability in the company. These changes were deemed successful by the investment company, why they designed an acquisition model claimed to encourage their continued involvement with the company. Economic incentives were established, aimed at retaining key managers, additionally, the company was acquired in two separate steps. In the first year 60 % of the shares of the company were obtained, followed by the remaining 40 % the next year (excluding minority shares held by key managers). The investors further claimed that another reason for this dual acquisition model was to ensure the continuing success of the company, after the investment company's initial entry. Their main goal for the company was to expand globally, through a combination of organic and inorganic growth.

#### Initial Actions

The investors' initial made some adjustments to the board, which was expanded to include three senior business developers from the investment company. Most of the previous members, including the previous owner, remained in the board. The previous chairman was asked to stay on as chairman, a role he was to keep for the following 4-5 years. Instead of rushing change and a new strategy, the investors claimed they wanted the time to learn more about the company from the inside and through the board. Why the investment company took on a fairly laid back role in the first six months after the Acquisitions. Which was enabled by the stabile structure and organization that the managers had created, according to the investors. They instead focused on supporting the company with their industrial know-how and past experience. Support that came mostly from the senior board members, whom had vast experience from leading large industrial corporations globally.

Some of their initiatives launched after the first six months, or as a reaction to their support was focused on some specific activities, primarily related to: pricing, patents, currency risk and tax optimization. The tax-structure and currency exposure were adjusted at an early stage. Where the tax-spend was slightly reduced through the inclusion of the company in the investment company's corporate structure. The currency risk was reduced and cost related to their previous risk adjustments could be reduced thanks to the investment companies experience the field. Something that was improved further through the beneficial agreements that the investment company was able to make between banks and the company. They also initiated

assessments of the company's patents and pricing strategy, areas that came to be some of the board's key focus areas during the following years.

#### 4.3.2 Part Two:

### New Board practices and Focus on Growth

#### Changes in the Practices of the Board

When the first half year had passed, the investment company took on a more aggressive role in the development of the company, taking on a more active role in the board, and changing the board's agenda and practices. The board therefore came to focus on the company's global growth and operational efficiency, where they wanted to ensure that the margins were kept high despite growing at a fast rate. To further help the board to understand the markets' movements, internal market studies and analysis were initiated. During this period the board came to gather between 4-8 times each year, which differed based on their perceived need for any additional meetings apart from their four ordinary gatherings.

With the entry of the senior business developers, the swiftness and confidence of the board was increased significantly, according to previous board members. Their experience helped to steer the board's focus to the key strategic questions at hand, where less time was spent discussing operational day-to-day duties, or in unnecessarily time consuming discussions. The previous board members claimed that this stronger focus helped accelerated the pace at which new directives and activities were implemented. Where stricter deadlines and a new "more action less talk" attitude was created. Despite this swifter and more actionable attitude, the atmosphere was kept open and down-to-earth. Which previous managers and board members claim to have made them more confident when discussing critical issues with the board.

The investors established new reporting routines consisting of three reporting stages, that were meant to help the board when monitoring Large.Corp's development. The first reporting stage meant that Large.Corp had to submit updates on key projects and key figures on a monthly basis. Where the key figures included an updated income statement, balance sheet, order intake and backlog. This was in turn followed by a short analysis at the headquarters of the investment company. The second reporting stage was the board meetings. Where a more more detailed report was required 5-7 days prior to every board meeting, which was to include requested analysis on key focus areas. However, according to the investors, the third and most important stage was

through the close ties between the chairman of the board and the CEO. Whom on a weekly and sometimes daily basis discussed order intake, important events or any concerns associated with the company. The relationship between the CEO and the chairman was intended to work like that between a mentor and mentee, characterized by an open and supportive relationship. Where the frequency for these dialogs depended on the urgency of the situation at hand. According to previous board members and managers, this practice enables the investment company to keep constant track of the company, allowing them to act swiftly if a negative trend were to show. However, they further claim that, one of the most important benefits of these discussions were not to keep track of the company, but rather to share experience with the CEO, and support him when transforming the company. Representatives from the investment company claimed that they intended for the company to be developed without too much operational involvement from the board. Where their goal was to act forcefully when needed, but allow the managers to develop the company themselves when possible. Hence the reports were claimed to be mainly used to know when not to bother the company unnecessarily.

Growth, through market expansion

With the increased involvement from the investment company came a stronger focus on developing Large.Corp's market presence and with it, their distributors and own salesforce. The company had grown through a series of partnerships with local distributors, as well as organically through fully-owned sales offices. Both of these groups were now targeted and granted extensive sales training to increase their efficiency, which was combined with the recruitment of additional sales representatives. The result was an increased capacity in their global salesforce, both in terms of total number of sales people, as well as an overall improved organization.

After having strengthened the salesforce, the company came to focus more on inorganic growth through global acquisitions. Something that differed from the previous strategy favoring organic growth. The company started evaluating potential acquisitions among: distributors, suppliers, and adjacent product groups. Of these groups, the distributors were found to be the most interesting, why an aggressive acquisition strategy of key distributors was formed. Soon many of their main distributors had been acquired, granting them a stronger market presence, leading to increased sales levels in all markets. They also chose to expand their market reach by increasing their presence in new emerging markets such as South America, Asia, and the Middle East. This expansion was made through a series of partnerships

with local actors, which previous board members claimed to be highly successful in granting them a fast expansion pace and access to valuable market knowledge.

Existing offering in new markets

Another part of the company's growth strategy was to introduce their current product offering to new market segments. Prior to the acquisition, Large.Corp had started investigating alternative segments, which received renewed focus with the help of the investors. At the time of the acquisition, Large.Corp was highly dependent on one main market segment, representing more than 95 % of their sales. New segments were quickly analyzed and introduced, in order to increase revenue streams and reduce their dependency on one single segment. Their offering was well received by the market, and within a few years it had resulted in increased sales and reduced dependency on that single segment. As of today, their original market segment still represents the largest share of their sales. However, its share of their total sales has been reduced from 95 % to 50 %. A change that the board members claim to have been enabled by the previously developed salesforce. Which had been restructured to implement a new segment-based sales model.

Product development and product expansion

Parallel with Large.Corp's market expansion, the company has invested a lot of time and resources in attempts to broaden their product portfolio. They have invested in RnD both internally and through external partnerships, with the intent of developing adjacent product lines that could be sold within their strong brand. Large.Corp also investigated similar products sold by competitors, in order to find out if they could pose an interesting acquisition target. However, these activities turned out to be unsuccessful. The research projects failed to deliver any new viable product opportunities. According to previous board members and managers, the products sold by the competitors were determined to be cheaper and inferior and therefore not considered a good match to Large.Corp's premium products. Even though the initiatives were unfruitful, they clearly show how Large.Corp have attempted to grow the company through both market and product expansion. It also demonstrates how highly they value the premium brand and strong positioning, resulting in their lack of will to pursue growth through an acquisition of a low-cost competitor.

Production

Large.Corp produces their own products via fully owned manufacturing plants in Sweden. According to previous managers and board members, these

manufacturing facilities were highly automated at the time of acquisition. Since then continuous investments have been made to ensure a highly cost efficient and reliable production. Which has been increased further new investments meant to increase their overall capacity as a response to their increased sales levels. However, the main concept and strategy for the production operations have remained the same, where the manufacturing is to remain highly automated and located in Sweden. Nevertheless, some initiatives have been launched, such as lean initiatives and projects meant to increase efficiency. According to the previous board members and managers, these initiatives resulted in reductions in working capital and capex, thereby increasing their profit margins. Which was further aided by their growing sales volumes, where scales of economy further helped them in improving their profit margins.

#### Logistics and sourcing

According to previous board members and managers, Large.Corp had already initiated a transformation prior to the acquisition. A transformation mainly focusing on improving the structure of the company, becoming more industrialized. The company had grown across the globe, resulting in higher strain on their supply chain. Therefore, the newly appointed board wanted to focus on improving the company's supply chain according to board minutes from the time. To ensure that it would be capable of handling their growing sales levels. One of the key improvements that was made was the recruitment of a dedicated supply chain manager, whose single focus was the development of their logistics and sourcing practices globally. Other tangible activities launched include: implementing currency hedging, challenging current suppliers to cost, and implementing a dual sourcing strategy. These activities combined with the renewed focus from the supply chain manager helped the company to improve significantly, according to board members and managers.

According to previous managers and board minutes, the dual sourcing strategy was particularly successful. The initiative lead to an overall decrease in the number of suppliers, and the review of the supply of strategic components. These specialized components had previously been sourced by one single supplier, which was soon changed by including another strategic partner. The decreased number of suppliers lead to higher volumes per supplier, which allowed the company to set higher demands on the suppliers. Through new negotiations the company was able to both decrease spend and increased delivery reliability. The added strategic supplier on the other hand reduced their sourcing risk towards their previous sole strategic supplier, and

came to increase their negotiation power. Another sourcing initiative launched was the assessment of risk connected with the ownership of the blueprints to their subcomponents. According to previous board members, the board soon learned that some strategic partners owned the legal rights to the blueprints of some components, through historic unfavorable agreements. This was soon changed to reduce this possible IP-risk, which however led to increased short-term costs. The dual sourcing strategy and review of IP-risks were initiated by the board, demonstrating their involvement in some operational issues.

#### Intentional exclusion of service

Large.Corp did not offer any service agreements to their customers prior to the acquisition, nor did that change with the new owners. Service agreements were discussed during a small number of board meetings, since service agreements and maintenance could potentially lead to increased revenue streams. However, the initiative was considered too risky due to their products' nature, according to board minutes. Their main product is a high-end component used for increasing the safety of the end product. It was decided that servicing these components could lead to legal-risks if the newly serviced products were to fail. A decision that was supported by the high costs that the service agreements were expected to result in, which was expected by the board and managers to result in modest profitability at best.

#### Pricing Strategy and Positioning

According to managers and board members, Large.Corp's product offering is considered by the market to be superior to that of their competitors'. Why their pricing strategy been shaped to reflect that increased perceived value, resulting in higher prices. Despite this relatively high price, their customers still consider the deal to be beneficial. Since the increased performance of the product leads to a lower total cost of ownership. The product itself is only a minor subcomponent of a larger end product, it is therefore not one of the customers' main cost drivers. This further helps the company maintain its high prices since the component is not in focus when their customers trying to reduce the overall cost of the end product. At the same time, Large.Corp's superior operations grant them lower production costs than that of their competitors. These lower production costs in combination with high prices continue to grant the company continued high profit margins. Ultimately, the board's determination to defend these high prices further explain why the earlier option of acquiring a low-cost competitor was turned down.

#### Intellectual Property rights

According to previous board members and managers, Large.Corp's increasingly global market presence set higher demands on their intellectual protection rights (IPR). Having the right patents have been extremely important when ensuring their continued strong standing, granted to them by their superior products. Prior to the acquisition the company had established some IP-protection and was in the process of evaluating the area further. The acquisition from the investor did however grant them access to experienced business developers, whom granted the area increased focus. One of the first activities initiated after the acquisition was to increase the number of global patents to include the markets that Large.Corp was currently operating in, or was planning to enter in the near future. They combined these patents with other sorts of IP-protection, building what previous managers refer to as a "protective web" of different sorts of design, process and product protection. Another benefit of this extensive setup was that they could increase the longevity of the patents, by adding on new layers of protection on patents that were soon expiring. Through this complex set of brand, product and process patents, the company built a very solid IP-protection. Which they have aggressively enforced through a series of legal disputes, further deterring any future competitors from violating their IPR according to board minutes and previous managers. Furthermore, IPR has gotten a lot of attention from the board and senior management, even resulting in the recruitment of a dedicated IPR-manager. IPR was also one critical aspect investigated in the due diligence process for the acquisition. Where a fundamental IP-protection was considered necessary for the acquisition to even take place according to investors at the investment company. However, these activities have been very costly, which goes to show how highly the company and the investors value strong IP-protection.

#### Investments and financing

The investments made in sales, IPR and production have been financed by a conventional mixture of own equity, gained by Large.Corp's stable cash flow, in combined with bank loans. The investment company have acted as a strong financial backer which have helped them renegotiate agreements with their banks to allow for more favorable terms, according to investors at the investment company. The largest portion of the financing for the company's investments have been from own equity, why the company's equity ratio has never been under 40 %. This has of course been supported by the company's strong profitability, still, it should be mentioned that previous board members have pointed out that they were very determined to ensuring the continued



financial stability of the company. Rather than leveraging the company's finances aggressively.

HRM, Remuneration and Incentives

According to previous managers, Large.Corp has focused a lot on internal recruiting, both before and after the acquisition. New talented people have been groomed over time to be readied to succeed senior managers and succession has been frequently discussed on board level. This has been done to ensure that the company would be prepared for any future changes in management, as well as monitoring upcoming talent. The practice has helped the company build a strong organization with talented individuals ready to fill any holes in the organization, which was on multiple occasions in the following years. During the first three years, a few senior managers left the organization. Most of them left due to personal reasons, however one was forced to leave due to lacking competence. Thanks to their succession plan, they could all quickly be replaced with competent people from within the organization, ensuring business as usual despite some significant changes. This practice came to include their acquired subsidiaries. Where the board initiated changes in management between the some of their different subsidiaries, meant to spread competence and best practice. According to previous managers and board members, this practice was very successful and lead to significant increases in sales of around 300-400 % in their Chinese sales office.

According to previous managers, Large.Corp did not have any particular incentive programs in place prior to the acquisition (excluding the fact that the previous owner was involved in the company). This was however swiftly changed on the initiative of the investment company. A program was designed to include senior management and key personnel, and soon came to involve 10-15 employees. Some minor bonuses were also granted for senior managers, incentivizing them to certain KPI:s connected with sales growth and profit margin. According to the investors and board members, the overall salaries for the managers should be considered average when compared to peers at similar companies. Where the incentive programs were designed to support a pay-for-performance structure, rewarding the best performing managers rather than having generally high salaries.

Taxes

According to the investors and previous board members, experience from the investment company helped Large.Corp in setting up favorable tax structures for their growing global organization. One of the main activities was focused

on centralizing their tax base at Large.Corp's headquarters in Sweden, rather than having it spread across their global subsidiaries. In doing so, excess profits and losses from their individual subsidiaries could be evened centrally, as well as towards the investment company's other portfolio companies. According to the investors this helped the company in reducing their tax spend. Another aspect that they revised was their transfer pricing setup, meaning how their internal prices between subsidiaries effected their tax base. A new structure was formed were most of their profits were allocated in Sweden, which have a relatively low corporate tax at 22 %, lower than the EU and OECD average. However, it should be noted that Large.Corp's tax practices are far from aggressive, where tax-havens and other complex structures have been avoided (Ekonomifakta, 2016).

### 4.3.3 Part Three: The Financial Crisis and Future Outlook

#### The Financial Crisis

Large.Corp had been owned by the investment company for a number of years before the financial crisis 2008, which came to be the first real challenge for the company. The company's situation before the crash was characterized by growth in all sectors, with new sales records being set year after year. Which in turn had caused them to invest heavily in the organization and their production capacity. When the crash hit the company quickly took on a more defensive role, readying itself to be able to initiate strong counters to what was expected to be a strong downturn in sales. The company developed a series of what-if scenarios, prepared cost-cutting programs and production initiatives. Activities that would allow them to quickly reduce working capital and unlock liquidity if need be. This resulted in the development of a program called "sharpening the blade", which identifying different cost-cutting measures that could be made on all levels of the organization. The program was designed to be modular, with different actions corresponding to a certain decrease in sales, stating what to do given a decrease of 10, 20 or 30 %. The program was made in detail, for example stating whom was to be laid off, and what production lines where to be closed or reduced. Activities that were described in detail by previous board members and managers, as well as in historic board minutes.

Whilst preparing for the worst, Large.Corp also launched activities to reinforce their great corporate culture that they had built over the years. During the crisis, regular public meetings were held with the entire workforce, ensuring that the employees were informed continuously on the

status of the company. According to previous managers, this stream of information helped build a unified front, where the employees helped by doing what they could to counteract the feared downfall.

During the fiscal year of 2009-06 to 2010-06 Large.Corp experienced their only historical decline in sales, which came to amount to no more than around 5 %. The company launched a set of initiatives to counter the decrease, including reducing overall production, reducing working capital through more lean production lines, and halting most planned recruitments. However, since the sales was considered relatively minor they chose not to lay off a single employee, wishing to keep the organization as strong as possible in the event of an upturn. Five years later, sales had grown by 100 %, where the intact organization helped the company to respond to the quick changes in the market, according to previous managers. The situation clearly demonstrates the board's will to invest in the company, as well as their swift handling in the face of a crisis.

#### Moving Forward

In summary, Large.Corp has been developed into a highly successful company, with strong increases in turnover, profits, market presence and number of employees vastly exceeding the industry average. This has been achieved by building on the strong foundation that Large.Corp had already built, as well as adding experienced business developers. Through a low risk profile, low debts and proactive activities during the financial crisis, the company has remained solid despite a turbulent global market. Where significant investments in production and sales capacity have paid off. As of today, Large.Corp is larger and more profitable than ever and 2009 remains the only single year that the company has experienced a decline in sales. Where new business opportunities and distributors are constantly being assessed in order to continue the growth of the company.

## 4.4 Auto.Corp

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Auto.Corp has been owned by the investment company for around two years. Since then, great changes have been to the organization in order to strengthen the company and allow for future acquisitions. The main activities issued by the board and senior management will be presented in three different parts. The first stage covers the first quarter, the second part the following two years, and the third part covers some future outlooks for the company.

Key Figures for the Company	
Industrial manufacturing company	
Industry:	Automotive
Turnover:	100 – 500 MSEK
Growth last 5 years:	2 % CAGR
Employees:	100 – 200
Avg EBITDA:	5-15 %
Reach:	Global sales
In portfolio:	Around 2 years

Figure 18: Key Figures for Auto.Corp

### 4.4.1 Part One: Initial Assessment and Actions

#### The Company and the Business Case

The investment company got to know Auto.Corp through two previous business partners, whom they had worked with together in previous projects. They proposed a joint acquisition model where the business partners were to acquire 30 % of the shares in Auto.Corp and the investment company were to acquire the rest, thereby becoming the majority shareholder. Due to the investors trust in the business partners and their track record from previous projects, the investment company decided to acquire the company. Prior to the acquisition, the company had been publically listed and was therefore delisted as a part of the acquisition.

According to both the investors and the business partners, the fact that Auto.Corp had previously been listed had resulted in a sparse ownership structure. They further claim that the lack of prominent owners meant that not much requirements were placed on the board or the the management, which lead to deteriorating productivity. Something that changed after the buy-out

with its now focused ownership structure. A new board of directors was formed, where most of the board members were replaced with people from the investment company and the business partners, where one of the business partners were elected chairman. The board grew to include eight people, consisting of two employee representatives, three people from the investment company and three people connected with the business partners. The number of board members was considered by both investors and business partners to be too many, however it was deemed necessary due to personal reasons. According to the investors, their initial understanding of the company was that it had a sound underlying business case, but was underperforming due to mismanagement and the lack of active owners. The goal was therefore to improve the organization of Auto.Corp, as well as expanding the company through organic and inorganic growth. Where the product portfolio was meant to be extended through acquisitions.

#### The Initial Actions

The newly formed board set out to assess the company, in order to learn how to best develop the company. According to previous board members, they quickly identified shortcomings in the overall management and organization of the company. Which caused them to initiate an in-depth HR-assessment of the senior managers. Furthermore, they concluded that there were many areas of the company that showed room for improvement, including sales, RnD, procurement, finance and production. These shortcomings were mainly considered results of the underperforming management team, according to board members.

Despite the potential for improvement, the core business showed great promise according to board members. A new strategy was set, stating that Auto.Corp was to grow through series of acquisitions, primarily aimed at growing their product portfolio. However, they realized that they had a long road ahead of them in readying the organization to handle future acquisitions. Why the short-term goals of the strategy were focused on the improving the company's leadership and organization. This change was initiated through the replacement of the CEO, whom were found through the use of an executive search company. Furthermore, the board ordered a number of market studies from external consultants, where the goal was to find interesting acquisition targets. These studies gave the board further insights into the market, but failed in granting them any evident acquisition candidates. The board therefore decided to delay the identification of acquisition until after the organization had been improved.

## 4.4.2 Part Two: Reshaping the Organization With New CEO

### Initiating Change Through the CEO

According to current board members, a new and qualified CEO had been recruited, whom were primarily tasked with the development of the company's organization. Their role now came to focus on supporting the new CEO's restructuring work and defining the future strategy. The CEO's first task was to get to know the company, thereafter suggesting and initiating changes to improve the situation. After a month, the CEO held a briefing to the board, in which he gave an elaborate walkthrough of the company's situation, according to the board. He then laid out a plan for how he was to develop the organization during the following year, and how the previously mentioned shortcomings were to be resolved. This came to focus on four main focus areas: the restructuring and improvement of the salesforce, the improvement of the financial reporting, overall improvements to the operations and ultimately, the improvement of the senior management and the overall corporate culture.

The CEO received a lot a freedom and responsibility when developing the company, where the board members claim that they were determined to grant the CEO the ability to work at his discretion. However, they used the same reporting procedures as in Large.Corp, with three reporting stages including the close cooperation between the CEO and the chairman of the board. Thereby implementing a structure with frequent reporting between the company and the board, without too much involvement from the board. Which according to board members was done to grant the CEO a strong sense of resolve, and the board the insurance that the company was being developed in the right direction. Furthermore, the CEO claims that this structure has allowed him to focus on the work at hand, rather than wasting too much time on time-consuming reports. Something the CEO claims to be vastly different when compared to his previous experiences from working with commercial PE-investors, whom tend to require the CEO to follow a detailed plan stating what is to be done for the first 180-days. In addition to having to give detailed reports on a frequent basis. He further pointed out that such commercial PE-investors also tended to use management consultants to a much higher degree. Whom he claims can be a great resource, while at the same time risk taking up too much of the senior management's time, while at the same time being very costly.

#### Corporate Culture, HRM and Incentives

According to the board members, one of the main reasons for why the organization had deteriorated was due to how the previous CEO had governed the company. His leadership style favored a system where all major decisions had to go through him which in turn discouraged the rest of the management team to make own decisions or take initiatives. The new CEO was determined to quickly turn the situation around, enforcing a new leadership style meant to favor resolve and individual performance. The managers were given higher degrees of responsibility, in combination with new routines for following-up on their work.

The pay-structure and incentive model for senior managers was changed to support this cultural and performance oriented change. The previously flat base-pay structure was replaced with a dynamic structure, where parts of the key managers pay were to be determined through a set of performance goals. These were shaped individually for each manager, and came to be shaped based on the managers' impact on: sales improvements, profitability, and gross margin. The new CEO was granted stock ownership as a part of his remuneration. A model that was intended to include other key managers when the new organization had been developed, according to board members.

#### The Salesforce and a New Sales Structure

The salesforce was soon restructured to better capture the company's market presence and product offering. Previously, most sales managers had worked intertwined, partially lacking clear business areas and performance goals, according to board members and the current CEO. The CEO therefore developed a new structure together with the sales managers, aimed at granting the managers higher degrees of responsibility and clearer work areas. These changes resulted in a new structure, which according to board members, the CEO and a manager, granted the salesforce a much clearer focus, divided into new product groups, markets and customer segments. When the new structure had been set, the number of sales representatives were increased by 50 – 100 %. In contrast to previous layoffs and reductions issued by previous management.

When the structure and extended sales team had been put in place, the company came to focus on increasing their market presence and sales. According to the CEO a lot more effort was put on developing emerging markets and developing the pricing strategy. Where rebates were reduced and low profit products were to be given less attention from the sales representatives. Furthermore, the prices for the company's products' were

changed to better reflect the perceived value of the product, rather than its production cost. According to the investors, the new pricing model went from a standardized cost-plus methodology, to a more value based model. Regardless, the model still needed work in order for them to rightfully call it completely value-based. These changes in pricing and segmentation were made relatively recently, why it is hard to distinguish any definite results of these changes. However, the financials indicate slight increases in sales as well as profitability according to the board minutes and board members.

It should be noted that according to the board members and the investors, this structural change much resemble the restructuring needed when transforming smaller entrepreneurial companies into commercially viable industrial companies. Which they further claim to be highly uncommon for a previously listed company, with a turnover of around 100 – 500 MSEK.

#### Financial Reporting

According to board members and the CEO, the lack of follow-up and traceability was not only a problem for the sales function, but for the finance and economics function as well. The financial reports failed to grant the board and key managers sufficient insights into the situation of the company, why a new reporting system was ordered and implemented. This system came to be fairly expensive and cumbersome to implement. Which according to the investors and board members, was expected, due to the company's previously lacking capabilities. According to board members, this new system would allow the senior managers and the board to better monitor and analyze the company and its subsidiaries. It would also allow the company to better cope with future acquisitions.

#### Positive Effects from De-Listing the Company

Before the acquisition, Auto.Corp had been listed on one of the smaller Swedish stock markets. When listed, the company spent a lot of resources on ensuring compliance with the demands set by the stock exchange. Where the reporting requirements in particular had proven to be time consuming. When the company ultimately got acquired, these demands were lifted. The company could now instead spend that time on developing the areas needed, where the economic function now had time to improve their internal systems rather than solely focusing on the creation of reports. Systems that according to the board members, should have been implemented years ago. However, the investors further point out that the listing cannot be held accountable for all of their shortcomings in the economics department. Instead the lack of sufficient leadership was the main driver for the department's limitations.



Operational changes and RnD

The operational aspects of the company have also been developed, where the goal has been to increase the profitability of some of the company's less profitable products. Particularly one of the company's product groups has been suffering from deteriorating profitability. Which caused the board and the CEO to devote time and resources to improve the situation. Activities have been made to assess the situation and to come up with potential alternatives for improvement, however, these were recently launched and are yet to be implemented.

Another field that was targeted was the RnD department, which according to investors had devoted to much time in further developing products, or improving outdated ones, instead of responding to the needs in the marketplace. The company therefore lacked any new products, as well as a pipeline with new projects. Their focus was therefore shifted by the CEO on the initiative of the board, stating that they were to refocus their efforts on new products that were aligned with the future needs of the market, rather than improving old legacy products.

### 4.4.3 Part Three: The Future Outlook

Future Outlook

Since Auto.Corp has only been owned by the investment company for around two years, they are still in the midst of their organizational development. However, a lot has changed since the investment company's entry. According to board members and the CEO, the organization has been strengthened significantly. Which has been achieved after cumbersome process in which around 80 % of the senior management has been replaced. The organization is still being strengthened, where new routines and work processes are being put in place.

New manufacturing alternatives are being evaluated for the currently inferior manufacturing site, which will likely result in the complete overhaul of the operations, according to board members. Furthermore, the board has reinvigorated their efforts in finding possible acquisition targets. Where board members claim to have identified a number of potentially interesting targets that are to be assessed further.

## 4.5 Chem.Corp

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Chem.Corp was founded by the investment company, unlike the other studied cases. Since the start some 12 – 16 years ago, the company has been grown into a dominating actor in its field, with a profitability that greatly exceeds that of their competitors. The main activities initiated by the board and senior management are presented below in three different parts. The first part covers the business case and the initial year, the second part covers the rest of the first five years and the last part covers some notable events thereafter.

Key Figures for the Company	
Industrial manufacturing company	
Industry:	Chemical
Turnover:	750 – 1200 MSEK
Growth last 5 years:	11 % CAGR
Employees:	100 – 200
Avg EBITDA:	5-15 %
Reach:	European sales
In portfolio:	12 – 16 years

Figure 19: Chem.Corp at a glance

### 4.5.1 Part One: The Planning and Launching of Chem.Corp

#### The Company and the Business Case

Chem.Corp was founded by the investment company based on an idea received from two external business partners, whom had extensive experience from the chemical industry. According to the investors, the business partners had identified a niche chemical product with a relatively small market that showed un-tapped potential. The segment was relatively un-noticed by the larger chemical giants due to its small size, and was mostly served by local and regional actors. They firmly believed that the market could be successfully transformed through consolidation. Where profits could be easily increased by improving the efficiency of the current manufacturing plants and through scales of economy. According to the investors, the business partners approached them due to their financial strength and strong track record from previous acquisitions, in addition to their strong brand and well-known business developers.

The product that they had identified is a liquid based chemical that is required in large quantities by the society as a whole. Since the product is required in large volumes by the customers, the supply chain is characterized by high transportation costs. Furthermore, the number of suppliers is relatively low, why finding a cost-efficient supply of input materials is critical. According to the investors the market is characterized by disperse manufacturing spread across Europe, served by small local actors with an overall over-capacity.

Together with the business partners, the investment company developed a strategy aimed at aggressively acquiring manufacturers around Europe in order to consolidate the market. Their goal was to become one of the three top market leaders within their niche, in just five years. As well as having made at least two successful acquisitions in the first two years. Where the main strengths of the venture were to be the combination of industry-specific knowledge from the business partners, with the industrial experience from the investors. According to board members, this new industrial focus was expected to grant them a strong competitive advantage in this slow moving niche market. The project was primarily to be financed through loans from banks and from the investment company, providing a strong financial platform for the first acquisitions. Thereafter the venture was expected to finance itself mainly through its own cash flow, since the investors favor relatively low debt levels. A detailed list of potential acquisitions and partnerships was formed, consisting of six possible acquisitions and six potential joint ventures. Furthermore, the company were to challenge the current product offering of their competitors, by introducing new alternative and adjacent products. Products that the investors expected to become increasingly dominating in a matter of years, according to board minutes.

#### Initial Actions

The project was initiated through the acquisition of two European manufacturers, quickly granting them sales of around 50 - 100 MSEK. During the remainder of the first year a lot of focus was put on the development of the acquired manufacturing plants, implementing lean initiatives and operational improvements. A board was formed, consisted of five people, including the two business partners and senior business developers from the investment company. One of the business partners was chosen to be the CEO of the new venture, and the other took place in the senior management. Where both of them were included in a stock-ownership program. Furthermore, additional employees with experience from operational transformations and lean were recruited, to help accelerate the profitability of the manufacturing plants. Meanwhile, additional acquisition targets were assessed by the board,

the investors and senior management, which would lead to an increased number of acquisitions in the following years.

## 4.5.2 Part Two: Acquisitions and Operations in Focus

### Fast Organic and Inorganic Growth

During the first five years Chem.Corp continued with its aggressive acquisition strategy. Each of these years, one or two additional plants were acquired across Europe. Where both stand-alone companies and carve outs from larger chemical companies were targeted. Most of these carve-outs were acquired from companies wanting to focus on other more specialized product areas. According to an investor, their will to only focus on “fancy” product groups, lead them to miss out on this profitable opportunity, which the investors refer to as more “nitty-gritty”. A claim that demonstrates that the investors are not afraid of investing in operationally demanding niche ventures. Additionally, the acquisitions were accompanied by a joint venture, much similar to the other acquisitions with the exception of joint ownership. It was to be governed much like the other plants why it will not be discussed further. However, the investors and the board soon realized that the number of interesting acquisition targets were insufficient to sustain their ambitious growth plans. They therefore came to established a small number of own manufacturing plants, in markets that the board claimed to have favorable dynamics. Some factors influencing where these sites were to be located include: competition, proximity to customers and/or suppliers and markets showing un-tapped potential.

Through this combination of organic and inorganic growth Chem.Corp quickly established a strong market position, with operations in most larger countries in central and western Europe. Driven by the acquisitions, their combined sales soon reached around 400 – 500 MSEK. The acquisitions further helped Chem.Corp gain access to new personnel, as well as legal and environmental permits. Where the acquisition of such permits helped accelerate their growth, since such documents could take years to obtain.

### Shifting Focus to Operational Excellency

The company quickly grew from being a new challenger, to one of the dominant actors in its industry. However, their profit margins had not developed at the same pace as their sales, why the board and the management came to focus increasingly on their operational efficiency. According to board members and board minutes, lean initiatives were launched, combined with

overall improvements to their internal processes. The board members claim that there were much room for improvements when comparing the acquired facilities' operational efficiency to the larger companies that they had previously managed. However, they also pointed out that the situation at their acquired sites were similar when compared to the competitors' plants. Which they claim to have worked in their favor, since few had the operational experience available to them as Chem.Corp had. Additionally, they implemented dual sourcing at the facilities where it was geographically possible. Many of their manufacturing plants only had access to a single supplier, though in the instances where more were available, two were selected and developed over time. According to the investors, the dual sourcing strategy led to increased negotiation and purchasing power, leading to reductions in manufacturing cost and sourcing risk. Furthermore, they relocated some of their operations that were distant to both suppliers and customers. These were reestablished closer to customers and suppliers, where the reduced manufacturing cost led to overall profitability improvements, outweighing the costs incurred by the moving the facilities.

#### Pricing and Competition

Chem.Corp's customers' main purchasing criteria is price, and there is significant difference between Chem.Corp's products and their competitors'. However, since the transportation cost is their main cost-base, the production costs is highly dependent on the geographic proximity between the manufacturing plant and its customers and suppliers. Why it is hard for a competitor to compete on price without having manufacturing facilities close by. The investors claim that this works as an entry-barrier, since competitors are unlikely to establish new facilities due to the current over-capacity in the market. These barriers help the actors to keep the prices relatively high. Where the investors claim to work proactively to ensure the high price level to ensure continued strong margins. Where reduced production costs are turned into profits, rather than decreased prices.

However, they have not always managed to keep their prices high, where some markets' higher degrees of competition have led to price reductions. Apart from Chem.Corp, there is one additional large actor that started to develop their European market presence just a few years before Chem.Corp's launch. According to board members and board minutes, this competitor felt increasingly threatened by Chem.Corp's fast expansion, why they wanted to defend their position as market leader. They started to retaliate through allegedly illegal predatory pricing and rumor spreading, with the intent to have a negative impact on Chem.Corp's brand. According to board members

and board minutes, predatory pricing, or price dumping, was used in the local markets where both actors had neighboring facilities. Which was implemented to keep Chem.Corp from gaining market share. Predatory pricing means that the products are sold at an intentional loss to keep competitors at bay and is illegal in most European markets. Chem.Corp therefore took legal action against the competitor, strengthened by the board members' previous experiences from leading companies in similar situations. However, the competitor's action was hard to prove, and during the following years the competitor continued to dump their prices and Chem.Corp continuing to take legal action. Their legal actions were successful in some, but not all of these markets, leading to high legal costs on both sides. Regardless, according to board members the actions had the desired effect of defending Chem.Corp's overall brand, which allowed them to continue to grow in Europe.

#### Focus on Profitability Rather Than New Products

The new products that the company had previously planned to introduce were now launched gradually in different test markets. These products also came to effect Chem.Corp when evaluating potential acquisition targets. Where manufacturing plants with the capacity to produce these products were slightly favored over the ones that were currently unable. However, according to the board minutes these new products did not receive the traction that the board and the investors had been hoping for. Why they with time decided to focus more of their efforts to developing the profitability of their other core products.

#### Succession

When the first years had passed and the company started to grow into a larger corporation, the board wanted to ensure the continued supply of competent managers. Why succession came to receive increased attention from the board. According to the board minutes the current managers were assessed regularly, to try and identify any future needs for replacements in the organization. This was combined with retention efforts for key managers and the review of junior talented employees. The goal was to identify those that had the capacity to take on increased levels of responsibility and to ensure that they received the training and attention needed to develop.

### 4.5.3 Part Three: Continued Growth in Saturated Markets

#### Saturated European Markets Forced New Growth Plans

After the companies first five years, their sales and market presence had grown significantly. In the following years they continued to acquire new facilities throughout Europe, though at a slightly slower pace than during the first five years. The European market was slowly becoming saturated, where Chem.Corp and their largest competitor had captured the majority of the market share. Due to the increased saturation in the European market, Chem.Corp started to investigate new possible markets outside of Europe, according to board minutes. New geographical regions, such as the middle east and Americas were assessed and deemed interesting. These markets were entered through partnerships with local actors, where the board minutes claim that the reason was to avoid any cultural risks and gain market knowledge for specific markets. Today most of Chem.Corp's growth comes from new markets, which are expected by the board to be their main source of growth during the following years.

#### Weathering the Financial Crisis

One notable event in the company's history is the financial crisis, and how the company chose to respond to the turbulent market. The board minutes show that the company prepared for a feared downturn in the market. Though, these preparations were far from drastic, since they operate in a market characterized by low cyclicity. The board monitored the company closely during this period and they noticed that some suppliers and competitors with exposure to other businesses experienced harder times. However, despite the turbulence the demand for their products remained, why they chose to maintain their prices at previous levels. They soon came to learn that no forceful actions were needed, since both sales and profits were kept high. Previous board members claim that the company weathered the storm well, in preparing countermeasures but not overreacting to the situation. Which is further proven by their financial results in 2007-2010, where all years were characterized by growing sales and profits.

#### Further Risk Mitigation

During recent years the board has come to focus increasingly on mitigating potential risks, such as the ones imposed by regulatory changes. Most chemical products, including Chem.Corp's, are subject to close monitoring and regulatory interest on national and regional level. Since the company's main market is Europe, Chem.Corp need to be aware of any potential

regulatory changes enforced by the EU, such as the relatively new directive REACH. These regulations are yet to have a significant negative impact on Chem.Corp directly, since their products are not harmful for neither humans nor the environment. Nevertheless, the company is highly dependent on the suppliers and customers close to their manufacturing sites. Whom may very well be effected by the directives which would in turn indirectly hurt Chem.Corp, where changes to the suppliers' or customers' situation could lead to decreased sales levels or sourcing issues. According to board minutes, the board therefore requires the management to keep close tabs on any potential regulatory changes effecting them or their stakeholders.

#### Future Outlook

Chem.Corp's history as a new venture demonstrates how the investment company has acted in a business case with no previous owner influencing the company's situation. Throughout its history, Chem.Corp's strategy has been characterized by an aggressive acquisition plan that was set on day one. Which has allowed the company to become one of the market leaders within its field in just a few years. The case further shows how past industrial experience can be used in entirely new industries. Where their strong focus on profitability alongside their growth has granted them EBITDA margins of around 15-20 %, previously unheard of in their industry. The future for the company is expected by the board to be relatively stable, where the new markets are considered promising but rather limited. Where their adjacent products on the other hand could potentially lead to increased sales levels.



## 4.6 Constr.Corp

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Constr.Corp is a specialist supplier for the construction industry that is being expanded throughout the Nordics. Since its acquisition around two years ago, the investors' main focus has been to develop the company's organization. Allowing them to hasten the expansion and potentially grow their product portfolio through acquisitions. The main activities initiated by the board and senior management are presented in three parts. The first one covers the business case and the first half year, the second part covers the rest of the two first years and the last part presents the current situation and future outlook of the company.

Key Figures for the Company	
Industrial manufacturing company	
Industry:	Construction
Turnover:	100 – 500 MSEK
Growth last 5 years:	N/A
Employees:	100 – 200
Avg EBITDA:	10-15 %
Reach:	Nordic sales
In portfolio:	Around 2 years

Figure 20: Constr.Corp at a glance

### 4.6.1 Part One: Restructuring and Expanding in Sweden

The business case

Prior to the acquisition, Constr.Corp was originally a niche business area of a large construction company in Finland. They had recently established a sales office in Sweden and the business area had a turnover of around 50 – 150 MSEK. Constr.Corp is a supplier and service provider to the large and medium sized construction companies and they offer what the board claim to be a superior product and service. When Constr.Corp was acquired by the investment company, it was bought as a carve-out, separating the business area from the rest of the corporate parent and launching it as a separate business. Constr.Corp was placed into a new holding company, where the national subsidiaries were placed in separated companies controlled by the holding company. The previous owners were asked to remain as a co-owner, retaining a 15 % stake in the finish subsidiary, a share that they continue to

control today. Where the investment company controls the rest of the shares (excluding minor shares owned by managers).

The company distinguishes themselves through their pricing and quotation process, that differs from that of their competitors. Constr.Corp charge their customers per unit produced, measured based on the size of the construction site and can therefore offer precise quotations before even starting. Which according to the investors grants them a substantial advantage to their competitors whom charge their customers on an hourly basis, much like most actors in the construction industry. The model also grants the company strong incentives to improve their efficiency continuously. Furthermore, they have designed their reimbursement model so that employees are paid per unit produced. Which in turn enable skilled workers to be paid significantly higher than the industry average. The investors further claim that this reimbursement model helps build a performance driven culture, claimed to be vastly different when compared to the rest of the construction industry.

According to the investors, there were two main rationales for acquiring the company. The first one was to grow the company in Sweden and to expand throughout the rest of the Nordics. The second rationale was to expand their product offering, adding on new products through future acquisitions. These acquisitions were considered important both to grow their sales, as well as to become a larger more strategically important supplier to their customers.

#### Initial Actions

The organization and senior management of the company was reshaped, where the organization was to be built around country specific subsidiaries, with CEOs of their own. In addition, a new group CEO was recruited, tasked with the overall management of the company. These senior managers were offered stock-ownership programs at group level. Which according to the investors was done to incentivize them to help benefit the group as a whole, not only their individual subsidiaries. A new board was formed, consisting of senior business developers from the investment company where the board's work where to be focused on the planned growth journey. The investors and board members claim that they quickly shaped the structure of the company to resemble that of a larger industrial company. A structure that would allow them to handle the fast-paced expansion, as well as any future acquisitions or extensions to the product portfolio. Furthermore, the sales function was extended and restructured. Previously, employees had worked both with sales and manufacturing, which the the board set out to change by developing a dedicated sales function. Additionally, more sales representatives were

recruited, which resulted in increasing sales that came to require additional recruitments for the production and logistics functions.

## 4.6.2 Part Two: Expansion and Reshaping Management

### Expansion Across the Nordics

After the initial restructuring of the company, Constr.Corp was quickly expanded in Sweden. Where a number of new sales offices were opened. The organization was strengthened further, where additional employees were recruited for the sales, logistics and manufacturing functions. Furthermore, several initiatives were launched aimed at developing the company's structure and support systems. Some examples of these initiatives include the implementation of a company-wide code of conduct, the strengthened of the HR function through the recruitment of a HR manager, new sales routines and employer branding activities.

The company simultaneously launched its expansion into Norway. Where a new regional CEO was recruited, initially tasked with the establishment of a sales office in Oslo. The office was primarily to work as a sales channel, whilst assessing the market. Where the initial jobs were to be performed by Swedish employees, before reaching sales levels high enough to justify the recruitment of manufacturing personnel.

The expansion in Sweden and Norway has mainly been financed by the company itself using regular bank loans and retained earnings. Where the relationship between the investment company and its banks has granted Constr.Corp access to beneficial deals and relatively cheap debt.

### Pricing

In order to further increase the company's turnover, the company has strived to increase their prices across its subsidiaries. In their original market, Finland, the prices were initially set at a low level to attract new customers. However, these customers quickly grow accustomed to the initially set price. A price that according to board members, has been hard to increase retaining customers. Therefore, the prices have been set at higher levels from start in the newer markets Sweden and Norway. Despite the higher price, the company has been well received, which according to board members, has granted them higher margins and turnover. These prices were set to match the perceived value granted by their offering, as opposed to the lower cost-plus

model used in Finland. Which has been much more successful according to board members.

Troubles with management

The strategic plan set by the investment company was according to board members fairly straightforward: recruit a strong management team, support the company through the board, and grow organically throughout the Nordics and through acquisitions. However, Constr.Corp quickly ran into difficulties whilst implementing their plan. The fast expansion pace has required them to recruit many new senior managers, where the group CEO and the regional CEO of Sweden turned out to be a mismatch for the company's aggressive strategy. According to the investors, the Swedish CEO lacked the resolve to perform the investments needed for maintaining a fast expansion pace. Which was believed to be partially accredited to the manager's incentive program. The manager appeared to lack the will to invest in initiatives resulting in increased cost, which in turn would lead to reduced rewards from his incentive program. These costly investments were however considered by the board to be necessary for the company's expansion. The board claim that they initially tried to resolve the issue, though it eventually became clear that the person needed to be replaced. His duties were to be taken over by the group CEO, with support from middle managers at the Swedish office.

However, shortly after having fired the Swedish CEO, the board was made aware of some managers' growing concerns regarding the group CEO's ability to lead the company. The relationship between the middle managers and the group CEO had quickly deteriorated, which created urgent leadership issues. The situation was immediately evaluated and was determined to be severe enough to require the person's replacement. The board claim that the issues were severe, why they quickly needed a new leader whom could help re-stabilize the the situation. A manager from the finish business partner, with previous knowledge of the organization, was recruited to lead the company as interim group CEO. According to board members, his previous knowledge of the company and personal ties to some of the employees would allow him to quickly address the situation. He was to remain group CEO and responsible for the Swedish division until a replacement could be found, thereby leading both the Swedish expansion and the rest of the group. According to board members, the urgency of the situation required them to act quickly. Why the process of replacing the CEO took less than a week measured from the day that the board was made aware of the situation. According to the investors, the support and access to key personnel granted by the Finnish co-investors was crucial when quickly resolving the matter. The recruitment of an external

CEO would be both costly and time consuming, requiring time to learn about the new company. Which they claim would have delayed the company's expansion with up to twelve months.

### 4.6.3 Part Three: New Future Opportunities

#### Acquisition

The acquisition-based part of the company's strategy is still on the board's agenda, but they are yet to find a strategically significant acquisition target. However, one minor but interesting opportunity has recently been located in Finland. The company offers an adjacent product to that of Constr.Corp, and is partially owned by a current manager at the Finish organization. Why another driver for the acquisition is to resolve the potential issue proven by the fact that a manager have an interest in both the targeted company and Constr.Corp. The acquisition would also allow Constr.Corp to grow their capacity, with the help of employees from the targeted company, with somewhat different skills than that of the current workers. The company is small with a turnover of around 10 MSEK, why the acquisition is not considered by the board to be strategically significant. However, the acquisition would grant the organization experience from performing an acquisition why the the investment is considered to be interesting according to board members.

#### Future Outlook

As of today, the company's expansion in Sweden and Norway is well underway, with several new sales offices having been established since the acquisition. According to the board members a newly recruited group CEO is to be introduced to the organization momentarily, whom is also going to be responsible for the Swedish regional office. This new structure is planned to continue until the time that the entire organization has grown further, justifying the need for an additional member of the senior management. The organization is still coping with these changes. However, the recruitment of several new employees in sales and the support functions have allowed the company to continue with its day-to-day operations without any major setbacks. Regardless, the management issues have taken a lot of time and resources from the company and its board. Time that better could have been used to hasten the company's expansion and growth. Where the investors claim that the issues with management have cost crucial time when expanding the company.

## 4.7 Empirical Summary

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The different studied portfolio companies have been developed using a number of different actions. These actions show different similarities and differences, both in terms of how they were initiated and when. Some of the most notable activities have been noted in the following table. A rough description of when the activity was initiated has been noted, measured as time after the acquisition. This notation has been done to further allow for a grouping of the activities, based on when it was initiated. However, it should be noted that the time-based notation only takes the starting date into account, why the duration of the activity cannot be seen in the following table. Nevertheless, this information will be presented and discussed in the analysis section, where a Gantt-chart of the activities will reveal the activities duration.

The blue fields represent activities initiated up to six months after the acquisition. The green field represents activities initiated thereafter, up to one and a half year after the acquisition. The orange fields represent activities initiated two years after the acquisition. This table will be used as a starting point when identifying the investor's development process.

Activities	Large	Auto	Chem	Constr
New Board	Day 1	Day 1	Day 1	Day 1
Financial Review	Month 1	Year 1	Day 1	Year 1
Tax & Compliance Review	Month 1	Year 2		Year 2
Assessing organization	Day 1	Day 1	Day 1	Day 1
Changes in Organizational structure and Management		Month 3		Day 1
Reporting Routines to board	Day 1	Day 1	Day 1	Day 1
Establish Sufficient Financial Reporting	Day 1	Month 6	Day 1	Month 6
Reporting and KPI:s for Senior Management	Month 6	Month 3	Day 1	Year 1
Incentive Programs	Day 1	Day 1	Day 1	Day 1
Reviewed Board Practices	Month 6	Day 1	Day 1	Day 1
Reviewed Sales Structure and Segmentation	Year 1	Month 2		Month 6
Increased Salesforce	Month 6	Month 6	Month 6	Month 6
Acquisition-Based Growth	Day 1	Day 1	Day 1	
Organic Growth: Existing Markets		Month 6	Year 3	Month 6
Organic Growth: New Markets	Year 1		Year 5	Year 1
Product Development/Extension	Year 2-3	Year 2-3		
Acquisition-Based Product Extension	Year 2-3	Year 2	Year 1	Year 2
Initiatives to Increase Efficiency in Operations	Year 1	Month 6	Month 6	Year 1
Reviewed Sourcing Practices	Year 2-3		Year 3	
IP Assessment	Month 3	Month 3		
Reviewed Pricing Strategy	Month 6	Month 6	Month 6	Month 6
Initiatives to Strengthen Corporate Culture		Month 6		Month 6
Succession	Year 3		Year 3	
Legal actions	Year 3		Year 3	

Figure 21: Summary of development activities

# 5 ANALYSIS

The analysis is divided into four distinct sections, where each section will cover different areas of an investor's development of a portfolio company. The first section will focus on the characteristics of the studied investor and how that may affect the developed company. Thereafter, the actions made in each company will be discussed, and how empirical data may differ from the theoretical data. In section three the actions made in each studied portfolio company is used when identifying different distinct phases of development. Phases that are used to unveil the studied investors development process. This process is refined and presented more thoroughly in section four, designed to highlight the most important focus areas for each phase. Hence, the sections will focus on different aspects of the framework that was developed in the theory section, where the numbering in the following illustration represents the area focused on in each section.

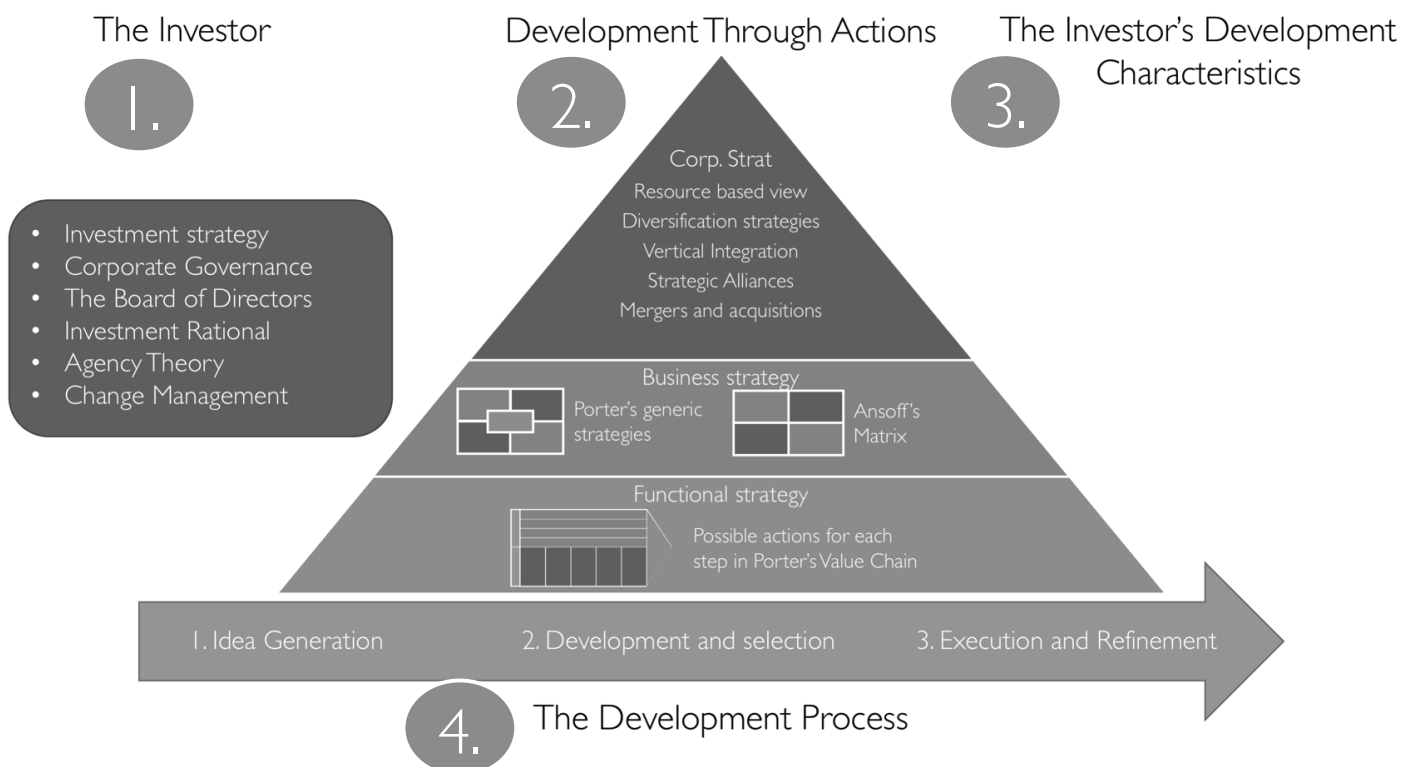


Figure 22: Each sections' corresponding level of the theoretical framework



## 5.1 Section I: The Investor

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In this section, the differences and similarities between the theoretical and empirical data regarding the investor will be discussed. The section will therefore focus on how the investor's perspective and characteristics can influence the development of their portfolio companies. It should be noted that the section *the board of directors*, as presented in the theory, will be included in this analysis' section: corporate governance.

### 5.1.1 Investment strategy

The investment strategy presented in the theory section covers factors such as: targeted industries, sectors, geographical coverage and holding period. These aspects often differ between actors and types of investors. The studied investment company is a private/family controlled actor, investing in a broad range of industries and sectors, excluding bio-tech and high-tech industries. They invest across the Nordics though tend to favor Swedish investments. The company does not typically have an active exit strategy and favor longer holding periods. Therefore, the company much matches the theory in how it presents some typical characteristics for private/family controlled companies. Especially due to the fact that they favor longer ownership horizons, industries from which the investors have previous experiences and investing in companies that are geographically nearby. They tend to use relatively low levels of debt, around 50 %, greatly differing them from their commercial counter-parts. Furthermore, they tend to favor profitable growth rather than aggressive growth. The profitable growth should be important for them as a long-term investor, since they live off the dividends generated by the company. Where an investor with a short investment period instead gains its profits from the successful sale of a company.

The longer holding period and the lower debt levels should allow the portfolio companies to be more stable, where lower financial costs and higher solidity grants the company access to future resources if needed. Which should allow the company to take more long-term oriented decisions, with less regard to their short-term effects.

In Constr.Corp's case, the decision to replace senior managers may have been less favored by an investors seeking a fast exit, since the replacement was estimated by the board to delay their expansion. However, pushing the company to hard could have had dire effects on its long-term stability. The

longer holding period does also help explain their actions in Large.Corp and Auto.Corp. In the stable company Large.Corp, the investors instead took on a laid-back role to learn more about the company. For an investor seeking a fast exit that period of time would likely have been more actionable, favoring operational winnings and other short-term actions. Regardless, their laid-back approach instead gave them time to focus on the long-term strategical decisions, which came to be highly successful in the long run. In Auto.Corp's case instead, this laid-back role can be seen in how they push for change through the CEO, when allowing him to reshape the organization as he seem best. The investment company favor working through the CEO, allowing him or her to build his senior management team. Something they believe will lead to a stronger organization in the long-term. A more short-sided investors could instead have chosen to reshape large portions of the senior management themselves. Which would likely have hastened the development of the company, at the risk of creating a less than ideal management team.

## 5.1.2 Corporate Governance

According to the theory, the Annual Shareholder's Meeting is one of the most central parts of the governance for a company with diverse ownership. However, in all of the studied portfolio companies the ownership structure is very clear, where the investment company controlling more than 70 % of the shares. This somewhat removes the need for a shareholders meeting since the will of the meeting is constantly represented through the investors in the board. Therefore, the meeting has a very limited role in the work of the investors.

The Board of Directors does have a very central role in all of the studied companies. It is through the board that the investors lead and develop the studied companies, why one of the initial actions in the acquired companies was to reshape the board. Thereafter, the investment company have little direct influence over the portfolio companies, which is instead done indirectly through the board, (where the investors may, or may not have chosen to take the seat as chairman). The boards' composition usually includes external representatives, why the will of the investment company and the will of the board does not necessarily have to be the same thing. The investors' majority ownership grants them the ability to enforce their decisions despite any different opinions. However, the investors claim that their representatives do not force changes without the support of the rest of the board, since the reason for them to recruit external members is for them to voice their opinions regarding the development of the company. The discussions held in between the board members was claimed to be very open and supportive by both

external and internal board members. Which illustrates the investors' ability to separate their roles as owners and board members, something the theory claim to be very important when having multiple roles at a company. Furthermore, the investors vast experience from leading companies via the board of directors does likely improve and accelerate the work made by the board. Where their efforts and time can be focused on what's most important at the time.

However, the boards' roles are not always strictly strategical. In Constr.Corp's case the board took on an operational role when assisting the company during the crisis period connected with the issues in senior management. Specifically, they supported the rest of the management with operational decisions, whilst at the same time looking for a replacement for the group and regional CEO roles. According to the theory, this is fairly common for a board of a smaller company, where their actions helped support their company. This example illustrates how much time and resources can be drained from the investors by a smaller company, where a smaller company can require as much time and resources as a larger one, given a similar maturity level. A larger company would naturally have a higher strategical capacity from their middle to senior management level, that could assist the board with the assessments or development needed. Where a smaller company may instead require the board to do some of that work. This can be especially problematic during a crisis, which could paradoxically mean that a smaller and lower valued company can cost more to develop than a larger company during a crisis. Something that needs to be considered by an investor when allocating resources to the different companies and when determining the composition of the portfolio companies' boards.

When examining the CEO's role in the different portfolio companies, it is apparent that he/she is expected to lead the operational change in the company. Where the board primarily is to have a strategic and supporting role. Hence, the CEO can be seen as the board's main tool when developing a company, where they guide and support the CEO through the chairman and through the rest of the board. As mentioned before, this is partially due to the investors' belief that a CEO whom is allowed to shape his management team to his liking, is better equipped to develop the company in the long term. However, their frequent reporting routines demonstrates their determination to keep close track on the companies. Where a CEO whom is unable to do what is needed, or that is unable to communicate the company's issues, will soon be replaced. The replaced CEO's in Auto.Corp and Constr.Corp demonstrate the investors' resolve after having identified issues, where their

laid back approach was quickly replaced with swift action at the sign of turbulence in the companies.

Apart from the reporting routines another way that the board ensures the competence of the CEO is through the initial assessment of the company. Here the CEO is assessed and according to the investors, one key area that the CEO needs to keep detailed track of is the company's key performance metrics, such as: turnover, order intake, profits and gross margins. If he or she is determined not to have full insights into that information, it would quickly raise questions regarding his or her ability to lead the company. Something that illustrates how highly the board values the communication and alignment between the CEO and the board.

Additionally, the communication between the chairman of the board and the CEO is very important, since it is through their dialog that the most frequent support is conveyed. It is crucial that this relationship stays open and honest so that the board's collective experience can be shared via the chairman on a frequent basis. This close cooperation between the CEO and board is barely covered in the theory. Why these practices have likely been developed by the investors to shape a model best suited for their individual investment practice. With that said, the investors pointed out that this practice is fairly common when examining other private or commercial investors. However, it is likely that the relationship is different when comparing it to investors with a shorter or more aggressive development and exit plan. Such aggressive plans often put higher requirements on the CEO, which combined with more aggressive incentive programs risk pushing the managers to the limit. In such a scenario, the CEO's incentives risk counteracting his inclination to share troubling information with the board, if the information were to have negative impacts on his or her short-term rewards. The studied investors' long-term strategy can instead encourage a more open dialog, where the cooperation between the CEO and the board would likely have a positive influence on the development.

In the theory, the auditor as one of the four entities of the corporate governance, has an important role when controlling the financials of the company. Furthermore, the theory points out that the auditor can often aid the company in the financial analysis and strategy forming of a company. However, for the studied investment company, the auditors of the different portfolio companies have a very limited role regarding the development of the company. The auditors are rarely mentioned in the board minutes or during the interviews, which indicates that the portfolio companies' auditors' main role is to ensure the compliance of the companies. The auditor's limited

role is caused by the investment company's lacking will to involve them in such strategical discussions. Likely since the investors' already have the required resources internally to perform such analysis, aided by the developers' experience. Furthermore, the developers require the companies to develop their financial departments so that the own departments are capable of doing the required assessments. Which reduces the need for external, likely costly, help from the auditor.

### 5.1.3 Investment Rational

The studied investment company is as mentioned a private/family controlled investment company. Since they invest their own capital, there is little need for them to inform, or take other investors' views into account, when managing their portfolio. This separates them from some, but not all financial investors, and allows them to develop the company without having to please other stakeholders, such as other shareholders. This scenario much resembles that of the commercial private equity actors, that grant their investors very little insight and control over the fund during the vesting period. However, the studied investment company have a very long investment horizon, which differs them greatly from most of the commercial private equity actors. The investment company's business model mainly revolves around getting income from dividends, as opposed to commercial actors with short vesting periods, whom get most of their profits from the successful sale of a company.

The investment company shows some resemblance to the industrial owners, regarding how they strive to administer and develop companies over long periods of time. Still, there is a great distinction between the two since the studied investment company develop a wide portfolio, rather than one corporate parent. Particularly since the investment company seldom strive to develop synergies between their portfolio companies. With that said, most of the business developers have vast experiences from leading such industrial companies/investors, why they likely share a lot of common practices in the operational development of their portfolio companies.

### 5.1.4 Agency Theory

The most commonly used incentive programs are presented in the theory section, including bonuses, share-ownership and stock-option programs. These can be altered in many ways, such as shaping them to grant greater benefits for reaching a certain goal, where aggressive programs are often used by commercial private equity companies. The studied investment company mainly uses relatively simple share-ownership programs, where the CEO and

other key senior managers are asked to participate. However, not at a level that would be high enough to risk the employee's personal finances. No aggressive alterations were used, nor were any stock-option programs used. In some of the cases, the share-ownership programs were combined with bonuses, tied to standardized key-metrics such as growth in turnover and profits. These fairly common programs seem to be valued highly by the investment company, most likely because of the programs' ability to motivate, retain and reward high-performing employees. Additionally, these standardized programs are likely connected with their ownership-horizon, where a simpler program would result in a more even reward system over time. It should in theory also have a lower risk of incentivizing the managers to act on self-interest. However, despite having a somewhat defensive program, the program still led to issues regarding the management team in Constr.Corp. Which goes to show that even a defensive program risk having negative effects on the performance of the company.

Ultimately, the investors pointed out that they ideally wanted to retain 90 % of the shares due to administrative and tax-related issues. Owning more than 90 % of the shares allow the investors to consolidate all their portfolio companies as a group. Granting them certain privileges that comes with governing a group of fully-controlled companies, rather than stand-alone minority investments.

### 5.1.5 Change Management

When studying the activities in the portfolio companies, there are several similarities between the actions made in the company, and the the steps from McKinsey's and Kotter's models. In both of the models, a set of preparatory steps needs to be made, to grant an understanding of the current situation in the company. Only thereafter can alternatives to development be prepared and evaluated. However, in all of the cases, the first actions include reshaping the board, and if necessary, the CEO and/or senior management. Something that was discussed by Collins when stating that you must first gather a strong team for the transformation, before determining how it is to be performed.

There are several differences between the process described in the theory, and the one that appears in the empirical data. In the empirical data, the initial assessing step seem to be followed by a direct readjustment stage, where the necessary change infrastructure needs to be built before evaluating and deciding upon the strategic options available to them. This was not covered in the theory which seemed to assume that such aspects were already developed. Another difference between the theory and the empirical data was

connected with the actions that were initiated as a response to extraordinary events, which was not mentioned at all in the theory. The empirical data showed that the reality can be much more complex than the theory, why there seem to be a need to include another step of the development process. This step should only revolve around the response to drastic external or internal events, something that can have a great effect on the planned development of a company.

Another difference when comparing the empirical data to the theory, is the theory's strong focus on communication, mentioned by both Jim Collins and Kotter. This communication is barely touched upon in the empirical data, likely due to a number of different factors. One explanation could be that senior managers and board members already take the need for communication into account when developing the companies, why it is not mentioned specifically by the board or board minutes. Another highly likely reason is the fact that this study has a central focus on the senior management team and board. Where the need for communication is mostly needed towards other parts of the organization, why it would go relatively unnoticed in this study. Instead the communication would be more of a preferred trait among the senior leaders of the portfolio companies, rather than an improvement area in need of development.

Ultimately, the investors' strong belief in their CEOs and key managers show great resemblance to Jim Collin's statements regarding strong management teams. Specifically regarding their belief that it is up to the CEO to form a strong senior management team with little involvement from the board. Furthermore, the rhetoric between the investors and managers indicate a very humble and personal connection, much in line with what Collins describe as a need for humility among the senior managers. One of the CEOs whom had experience from leading companies owned by both commercial and private investors claimed that the relationship between the senior management and board is much more open when owned by a private investor. Where the commercial investors instead lead by ordering, rather than discussing. This will of course differ from company to company, regardless, the humble approach from senior board members and investors likely strengthen the relationship between the companies and the investors, aiding the development of the company.

## 5.2 Section 2: Development Through Actions

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This second section of the analysis will focus on the development of the portfolio company, through the different actions initiated in the companies. Here the empirical data and theory will be compared to understand what potential areas of development are focused on by the investment company. This will be presented in the same form as in the theory section, based on the model: *levels of strategy*.

### 5.2.1 Corporate strategy

#### 5.2.1.1 Diversification

In all of the studied cases it is apparent that the investors have driven change aimed at increasing growth and profitability simultaneously. Diversification has been one way of reaching their goal, where new business areas and ventures have been investigated. All of the studied portfolio companies have been extended to increase sales and/or profits, by diversifying them based on market or product. In Constr.Corp and Chem.Corp, this has mainly been done by diversifying across new markets, reaching new customers within the same segments as in their core markets. However, Large.Corp has also expanded into new segments, not only to increase their sales and profitability, but to reduce their market risk as well, a factor that the theory claims to favor a diversification strategy. The investment company should be considered to focus primarily on growth, though this examples indicates that the risk mitigation aspects receive increased focus with increased levels of maturity.

Another aspect of the diversification strategy is concerned with how the investors seek to diversify their portfolio of investments. The studied investment company control a highly diversified portfolio of companies, why they according to the theory should primarily want to ensure the diversity of the portfolio, rather than for the individual companies. This may help explain why the risk mitigating activities receive less of a focus in the smaller companies, due to their reduced impact on investment company as a whole. However, if the company grows to represent a significant share of the investors' portfolio, then the need for risk mitigation should in theory increase. This may in turn indicate an increased level of risk-awareness in the larger companies, somewhat proven through the risk-mitigation activities in Large.Corp.



### 5.2.1.2 Vertical integration

Vertical integration has mainly been implemented in one of the studied companies, Large.Corp, where distributors have been acquired to increase their growth and market presence. However, there is a clear distinction between the theory and the empiric material regarding their rationale for integrating vertically. Large.Corp's main driver for integrating vertically was to increase their profits and sales. As opposed to the theory that focuses on factors such as securing access to sales channels or input material. Another critical factor that drove the investors' decision to acquire the distributors was their will to develop the salesforces of the distributors. Where increased control would facilitate training and segmenting actions. Which was an aspect that was barely touched upon in the theory.

It should also be noted that Chem.Corp show resemblance to vertical integration in how they have developed their operations through close partnerships with suppliers and customers. Some examples include relocating their manufacturing sites to decrease transportation distance and cost. Which was claimed by the theory to be one driver for vertical integration. However, this was done without joint ownership, or long-term contracts, proving that some of the benefits of vertical integration can be obtained without actually integrating.

### 5.2.1.3 M&A

The empirical material clearly demonstrates the investment company's preference for M&A, since acquisitions are made, or planned, in all of the studied companies. The reason for these acquisitions vary, and heavily depend on the industry dynamics for each studied company. However, one common criteria in all of the cases is to grow the sales of the company, which can be achieved in a number of different ways.

In Large.Corp's case the M&A strategy's main objective is to increase their turnover, why many different M&A targets were evaluated. Additionally, another important reason was likely to increase their market power and presence, why different acquisitions within that field were evaluated. Furthermore, the company also sought to grow their product portfolio, why several acquisition targets within new product groups were evaluated. Where such a product oriented acquisition would allow them to accelerate their speed to market as well as lower the cost and risk of developing products in-house. However, these benefits, as discussed in the theory section, do not seem to be significant for their decision to increase their product portfolio through M&A. The fact that they simultaneously increased their internal and external product

development efforts proves that they were more interested in finding new options, than keeping the cost down. Furthermore, the fact that most of their M&A activity came to focus on the acquisition of sales channels and distributors further prove that the product extension was not as central as the main growth target.

In Auto.Corp and Constr.Corp increasing the product portfolio has a much more central role than in the other companies. An increased product portfolio would grant both companies a stronger standing towards their customers and distributors, making them a much more strategically important partner. Hence, the market power argument is much stronger for these two cases. Fueled by the increasing requirements from their customers and their will to reduce their number of suppliers. Furthermore, the increased product portfolio was one of the critical success factors when acquiring the companies, further proving that the rationale for their M&A strategy depend more on the business case than an overall preference.

Chem.Corp much resembles the rest of the companies in how their acquisitions have allowed them to grow the company at a high speed. However, the other arguments such as “speed of route to market” and “overcoming entry barriers” must be considered critical. Since they managed to acquire the legal documents needed for their expansion, hastened their route to market significantly.

All of the cases illustrate how the investment company favor an aggressive M&A strategy, though shaped in a way best suited for each portfolio company. Since the strategy is so apparent and consistent, it must be considered one of the key characteristics of the investment company, likely attributing to some of their success. However, they still show evidence of wanting to grow the companies organically, evident in all of the cases. Therefore, the M&A strategy should only be considered one of the different growth options used in the portfolio companies. Furthermore, in both Auto.Corp and Constr.Corp, the acquisitions were put on hold for the first few years. Which indicates that the investors first want to evaluate other growth options, and ensure the readiness of the organization, before implementing an M&A strategy.

In the theory, acquisitions are claimed to fail more often than succeed, indicating the difficulties and challenges when implementing an M&A strategy. Considering the senior business developers experience from leading large M&A-oriented companies during the 80’s, these issues are likely the reason for their wish thoroughly evaluate the situation before implementing

the strategy. Experience that most certainly have granted them benefits when leading their portfolio companies through M&A strategies as investors and board members.

#### 5.2.1.4 Strategic Alliances

In the theory, there are many different reasons for entering strategic alliances. Some of these alliances, such as: franchising, vendor partnerships and long-term contracts, are connected with the operational aspects of the companies. Aimed at improving the sales channels or operations of the parent company. Regardless, such alliances were not identified in any of the studied companies. However, in Chem.Corp's case, one of the new manufacturing sites was acquired together with another business partner and developed as a joint venture. This joint venture was developed much like the other acquisitions, where the investment company had a lot of control in the development of the company. Therefore, it is likely that the joint venture was based on the seller's requirement to retain a portion of the company, rather as a mean of development, since no other alliances were formed.

When examining the portfolio companies, it is clear that the investors favor owning a majority share in their portfolio companies and subsidiaries, rather than developing them as alliances. However, an investor does not necessarily need to own more than 50 % of the shares in a company to have the controlling influence over the company. In companies with disperse and inactive ownership, it is often enough to own significantly higher amount of shares than the second largest owner, due to the difficulties associated with engaging minority shareholders. This sometimes mean that an owner in a listed company can have strong influence over the development of the company, despite only owning as little as 5 % of the shares. However, such conditions rarely apply in smaller private equity companies, why their wish to control at least 50, but preferably >70 %, is understandable. Owning more than 50 % allow the owners increased flexibility when inviting new business partners, or senior managers. Since they can retain their controlling stake despite handing out or selling some of their stock.

## 5.2.2 Business strategy

### 5.2.2.1 Porter's generic strategies

All of the companies offer diversified, quality products in niche markets and are clear examples of a differentiation strategy, as presented in Porter's generic strategy model. None of the cases show resemblance to a cost leadership strategy, likely due to the investors' lacking will to invest, or engage in price wars or price reductions. Some of the cases show indications of a focused differentiation strategy, where the companies chose to focus on a specific segment. However, in general the companies appear to want to develop a niche in a broader sense, instead of only focusing on a specific segment within that niche. Demonstrated by both Large.Corp and Auto.Corp when expanding their sales to new segments. Therefore, the companies rather appear to pursue a differentiation strategy, rather than a focused differentiation strategy.

Chem.Corp's case is somewhat different to the other, in how their strategy can be considered a combination of the cost leadership and differentiation strategy, since the customers favor the price leader, not caring much for a differentiated product. However, in their case, the strategy still mostly resembles a differentiation strategy. Though instead of differentiating themselves through their products, as in the other cases, they differentiate themselves through market presence. Utilizing the market barriers caused by the freight cost and over-capacity in the market. Furthermore, some of the local markets resemble a monopoly or oligopoly situation, eliminating or reducing the need to compete on price.

Overall, the investment company appear to never want to compete on cost. Instead they prefer to differentiate their portfolio companies either through their product offering, or their market presence. Through such a strategy they can ensure that the prices are kept high, granting the portfolio companies higher profits, in turn leading to higher dividends for the investment company.

### 5.2.2.2 Ansoff's Matrix

The Ansoff matrix is a tool used for mapping and evaluating a company's growth options. The first three steps of the matrix are all used or evaluated in each of the different case companies. For each of the steps, different methods of implementation are evaluated. For the matrix's product development square, the cases illustrate how external, internal and acquisition based product development have been initiated or evaluated. When instead

investigating the market development aspects for both new and existing markets, it is evident that both organic and inorganic growth was developed or evaluated. Since the investors value growth highly, this matrix can be seen to have a central role when developing their companies, where each option is evaluated based on the organization's capacity, the markets' characteristics and the potential profits for each option. This may seem self-explanatory, where the company should ideally develop the route associated with the lowest possible risk, and highest likelihood of success. Though, it is up to the board and senior managers to gather enough reliable data in order to decide which route best matches these criteria. It is therefore crucial to ensure that the company has access to the information needed for evaluating the different options, and developers that are capable of selecting the best alternatives.

It should be noted that the fourth square, the diversification strategy, is absent in all of the studied cases. This square differs much from the other strategies and is seldom pursued since it is often associated with high risks and relatively limited rewards. This may indicate that the investors favor a more reliable and gradual growth journey, rather than risky and aggressive initiatives.

### 5.2.3 Functional strategy

#### 5.2.3.1 Infrastructure Economy/finance

When comparing the theory and the empirical data regarding the financing of the portfolio companies, it is clear that there exist some differences between the two. All of the studied portfolio companies were early refinanced to have a 50-50 share of equity and debt. One reason for this refinancing was to renegotiate the companies' current agreements with their banks. Where the companies were instead included in the investment company's favorable agreements with its preferred banks, granting the portfolio companies lower financial cost. Another reason was to unlock capital from the previously equity financed companies, capital that could instead be invested in new ventures. In turn leading to increased risk for the portfolio and somewhat increased financial costs. However, these financial costs can for the time being be considered negligible, due to low interest rates and profitable agreements between the investment company and its preferred banks.

The 50-50 financing indicates that the investment company is willing to leverage their companies to some extent, in order to unlock more capital for further investments. However, the leveraging is held on a fairly defensive level, where a more aggressive commercial investor can be expected to favor a higher risk profile and higher levels of debt.

Furthermore, the investors have worked to restructure and improve the finance and accounting departments of some of the companies. Which was done to ensure that the departments were able to compile sufficient information regarding the company's performance. This partially meant increasing the granularity of the reports that were made, so that they would share more detailed information. This would in length allow the board to better monitor the development of the company. However, these improvements were only initiated after first dealing with the most critical issues at hand, such as reshaping the senior management or restructuring the sales function. This proves that the investment company's wish to develop their companies gradually by focusing on the most urgent issues at hand. This requires a great deal of industrial experience from the investor, being able to rely on more intangible information than the ones granted by detailed financial reports. However, it allowed the companies to better allocate their resources at an early stage, potentially increasing their long-term performance. This would likely have differed if the portfolio company would have been run by a financial investor, with less industrial experience. For such an investor, detailed financial reports are often critical when monitoring the company, why they would likely ensure the quality of the reports at an earlier stage.

#### 5.2.3.2 Human resources

The investors' involvement with HRM is mainly through the recruitment and remuneration of the CEO, senior managers, and the board. The investors claim that one of their most critical tasks is to recruit the right CEO, especially since they seldom influence the recruitment of other employees or managers. Furthermore, the CEO has a very central role in the development of the company, since he or she is expected to both implement the actions decided upon by the board, and to be able to communicate clearly with the chairman and the rest of the board. Therefore, the recruitment of the CEO is central for the development of the company and needs to be performed in the best way possible.

The CEOs for the portfolio companies were recruited in different ways, where previous business partners or previous associates with the right experience were generally proffered over external hires. When the investment company was unable to find such a previously known CEO they used an executive search firm. In these cases, one and the same firm was used repeatedly, to ensure that they got to know each other's practices and preferences regarding the candidates, which would facilitate future cooperation. Both of these

recruitment practices show how highly the investors favor their relationship with the potential employee or search firm. Since the recruitment of the CEO is so important, this is relationship-based recruitment practice is likely a way to reduce the risk of hiring the wrong people for the job. Where a previously untested employee or recruitment firm may pose more of a risk than someone previously known to the company.

All of the CEOs were granted moderate salaries, combined with bonus programs and share-ownership programs, as mentioned in the section on agency theory. The investors appear to want to promoting a pay-for-performance structure, that they ideally wish to be transferred to other parts of the organization. Furthermore, the programs were designed to align the interest of the senior managers with that of the investors. The theory favors the use of incentive programs though is undecided when discussing the programs from a motivational perspective. Regardless, the investors clearly have a preference for motivating employees through the use of incentive programs. Programs that for example helped drive change in Auto.Corp, creating a new performance-based pay-structure that helped shape a more resolute organization, with employees taking on higher levels of responsibility.

Lastly, the succession of senior managers was discussed in both Large.Corp and Chem.Corp, after having developed the companies for around three years. It appears that the board wanted to ensure the continued stability in the senior management team, after the companies had reached certain degrees of maturity and stability. Thereafter succession came to be a recurrent theme during the board meetings, discussed on a yearly or on a need-based basis. Succession-planning was briefly touched upon in the theory, stating the need for a developed talent and succession program. However, in the smaller companies, the situation was considered to be too unstable to launch and develop a succession program, likely since the current employee turnover is too great to grant any real results. Which indicates that succession planning and talent management should be implemented after having developed the more urgent parts of the organization.

### 5.2.3.3 Technology/Resource and development

The companies' product development and RnD departments have been developed by the investors to various extent, based on the companies' characteristics. The area has received little attention in Chem.Corp's and Constr.Corp's case, since they provide more of a standardized product, which is not expected to change much in the years to come. With that said, Chem.Corp has a well-developed product offering and are ready to increase the sales of new products as soon as the market is ready. Therefore, the area has currently been determined to be in little need of improvement.

For Auto.Corp, the area was quickly determined to be in need of improvement why initiatives were launched to develop the department and refocus it. However, this has not been a central focus for the early development of the company, indicating that the investors are more interested in broadening their product portfolio through acquisitions, rather than through internal development.

Lastly, in Large.Corp the department was initially determined to be well functioning and in need of little adjustment. In the following years the area received renewed attention due to their will to develop new products. However, these initiatives were combined with with external research efforts, which indicate that the investors only see the RnD department as one of the means through which new products can be developed.

All in all, the investors seem to want to ensure that the RnD department's focus is on the most value adding activities, though it not one of their most central areas for development. Which was based on an initial assessment of the area that was made in all of the companies. Additionally, the external research efforts and acquisitions show that the investors seek to evaluate different means to expand their offering, tailored for each company. Though such efforts are not at the center of attention and is often developed during a later stage of the development.

### 5.2.3.4 Procurement

The procurement aspect has been notably untouched in the cases, and has only been discussed briefly in some of the cases. The area does not seem to be in focus during the early stages of development and resources are instead allocated to focus on the more urgent issues at hand. This is particularly clear in Auto.Corp and Constr.Corp, where the development has been focused on the company's management and strategic issues, rather than operational improvements. Nevertheless, with increasing levels of maturity, the area



seems to grow in importance, notable to some extent in Chem.Corp through the implementation of new sourcing practices. In Large.Corp this was even more apparent, where a new supply chain manager was recruited to oversee the development of the operations and procurement. With that said, the area should not be seen as one of the most central development areas, where other more urgent issues such as acquisitions and growth initiatives have gotten a lot more attention from the senior managers and board. Which may seem surprising when compared to the theory, that stresses the fact that the procurement activities can have a significant impact on the bottom line.

#### 5.2.3.5 Operations, Logistics and Manufacturing

The operations and logistics activities received some initial focus in the studied cases, mostly connected with the overall assessment of the companies. Thereafter, not much was done within the field during the initial stages of ownership. However, when some time had passed, and with the increased knowledge gained by the board, the area came to receive a renewed focus in the later stages of the development. A focus that grew with increasing levels of maturity, why the larger companies' operations received more focus than the smaller ones.

For Chem.Corp and Large.Corp, this meant an increased focus on improving profitability and efficiency after two to three years, where initiatives such as the implementation of a dual sourcing strategy was implemented in both of the companies. For the smaller and less mature companies, Auto.Corp and Constr.Corp, these activities are yet to be focused on. Hence, the area is left for the management to develop, which has not been prioritized as highly as other areas. This practice much resembles the investors' development of the procurement function, that mainly received focus after having reached certain levels of stability and maturity. Instead the investors first seek to develop the sales, senior management team and other more urgent aspects of the company, before refining and trimming the operations. The same goes for the financial engineering that is often made at different levels of the operations. Little, if any, efforts are made by the investors to readjust financial figures connected with procurement or the operations. Something that many other commercial actors are claimed to do. The need for financial engineering should be much lower in a portfolio company that is planned to be held for a long time, which allows the company to better focus its time and resources to the most urgent issues at hand.

The theory firmly states the benefits of improving the operations, logistics and procurement areas, due to their strong correlation to the profitability of

the company. However, the investors decision to initially focus on other areas is likely connected with their long investment horizon and their preference for developing the companies through the CEO, thus not meddling unnecessarily in the day-to-day operations. The CEO is therefore expected to lead this development with the help of his or her senior management team, why some minor improvements may have gone relatively unnoticed during this study. Nevertheless, if such improvements were to have had a significant impact on the company, they should be expected to have been discussed by the board. Why any such operational improvements can only be expected to have been minor.

#### 5.2.3.6 Sales and marketing

In all of the cases, the investment company and the boards of the companies has required to invest in an increased salesforce, often combined with initiatives aimed at improving its efficiency. These activities are clearly in line with the investors' intent to increase the companies' sales, why it has received a relatively high focus in the early stages of development.

Furthermore, the investors drove change in the segmentation and structuring of the salesforce in both Auto.Corp and Large.Corp. Where the business developers likely reshape the companies to better resemble the larger stable companies that the developers have experience from leading. Based on the development made, these changes are likely going to allow the companies to grow their sales through the development of new segments. A structure that would help ready the company for its future growth journey, since it could be adapted to fit even larger sales volumes. However, the implementation of these improvement was left for the CEO, further proving the investors' and boards' deep reliance on the CEOs of the portfolio companies.

The pricing strategy of the companies is another area related to sales and marketing that has been developed in all of the companies. The areas have received a lot of focus from the board, with the goal of increasing, or keeping the prices high in all of the companies. Which for example caused Auto.Corp and Large.Corp to implement a new value-based marketing strategy. Before the acquisition, their pricing model had resembled a standardized cost-plus model, where the price had been set based on their production costs. Now the prices were instead set to better meet the perceived value of the customers. Product specific price adjustments allowed them to increase the overall price level, which lead to increased profitability since they managed to do so without losing any significant number of customers. Furthermore, products with low profitability were either phased out, or received a significant price

increase. Which either increase the profitability of that product, or steered the customers towards more profitable products.

These changes have in general lead to increased profits, and prices better matching the purchasing will of the customers. Which supports the investors desire to increase their portfolio companies' profitability. The actions initiated by the investors can be compared to the theory and the presented 4-P model, where it appears that it is mostly one of the P:s, Price, that is developed at board level. The other P:s are likely mainly left for the marketing and sales functions to develop.

#### 5.2.3.7 Service

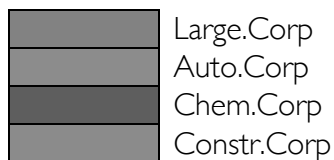
Service has only been briefly discussed in the cases, specifically in Large.Corp and Auto.Corp where it was seen as a potential alternative to increase turnover through the implementation of service agreements. Nevertheless, the service agreements in both of the cases were quickly determined to be associated with significant risks and issues. Furthermore, the profitability of the service agreement was determined to modest at best, which given the risks lead the companies to put the agreements on hold. In the theory section these service agreements were claimed to be highly profitable and beneficial when increasing sales. However, the success of service agreements depends highly on the industry dynamics for that product, why sufficient analysis needs to be made before launching a service offering.

### 5.2.4 Development Activities Over Time

The development initiated by the investment company appear to occur in different phases, based on the empirical summary. The actions initiated by the investors correspond to the period of time since the acquisition, and the maturity of the company. In the following table, the activities that were identified and summed up in the empiric summary, have been translated into a Gantt-chart, illustrating what actions were made during different periods of time. Period one (P1) starts at the time of the acquisition, and lasts for three to six months. Period two (P2) starts thereafter and lasts until one and a half, to two years have passed. The ultimate stage (P3) covers what happens thereafter, until the fifth or last year of ownership. The reason for the difference in period length is due to the differences in the companies. For example, the initial stage in Large.Corp was fairly long, when the investment company took on a laid-back and learning role for around six months. In Auto.Corp's case, this period was shorter, around three months, since changes in management were needed at a much earlier stage.



Figure 23: Gantt-chart illustrating the key development activities over time



## 5.3 Section 3: Grouping Individual Activities into Phases

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During this section, the identified activities are grouped into phases, based on the time and characteristics of the initiated actions in each company. These phases will each represent a crucial step in the development methodology used by the investors, in total five different phases are presented. Thereafter, the need for adapting the process will be discussed, since each company will be required to be developed in a way best suited for its industry, markets and characteristics.

### 5.3.1 Grouped Activities Translated into Phases

The concluding Gantt-chart presented in the second analysis section indicate that the activities performed follow a phase based plan. There are several actions that appear to occur based on time of ownership and the maturity level of the companies studied, which were grouped into three different phases. However, there are some activities that appear to occur based on other factors than the period of time and maturity of the company. These are based on extraordinary internal or external factors, such as the management issues in Constr.Corp, or the financial crisis' on Large.Corp and Chem.Corp. These particular activities are grouped together in a new category, called "Event-based", short for event-based activities. This new grouping, consisting of four different phases, will form the basis for understanding the development process of the investment company. This development process will in the fourth section of this analysis be translated into "development stages". These development stages will represent the what and the how of development strategy implemented by the investment company. These stages of development are partially inspired by the model designed by McKinsey & Company, which was presented in the theory section. However, these development stages are altered significantly based on the work made by the investor, to best resemble their prioritization and development preferences.

### 5.3.2 The Four Activity-Based Phases

The following schematic illustrates the four different phases that were identified by grouping the actions made in the four case companies.

Phase 1	Phase 2	Phase 3	Event-based
New board	Financial review	Acquisition-based growth	Legal actions
Financial review	Tax and compliance review	Organic growth: existing markets	Initiatives regarding corporate culture
Assessing organization	Changes in organizational structure and management	Organic growth: new markets	Cost-cutting programs
Changes in organizational structure and management	Establishing sufficient financial reporting	Product development/extension	
Reporting routines to the board	Reporting and KPIs senior management	Acquisition-based product extension	
Reviewed board practices	Reviewed board practices	Initiatives to increase efficiency in operations	
Establishing sufficient financial reporting	Reviewed sales structure and segmentation	Reviewed sourcing practices	
Reporting and KPIs senior management	Increased salesforce	Reviewed pricing strategy	
Incentive programs	Acquisition-based growth	Succession	
New board practices	Organic growth: existing markets		
Acquisition-based growth	Organic growth: new markets		
IP Assessment	Acquisition-based product extension		
	Initiatives to increase efficiency in operations		
	Reviewed pricing strategy		

Figure 24: The four activity-based phases

### 5.3.3 An Additional Phase is Needed

The four initial stages are all based on the activities initiated in the different portfolio companies. However, these four stages all rely on extensive assessments, where some are even made before the acquisition of the company. These assessments are used when forming the initial business case and strategic plan for the development of the company. Due to the importance of this initial assessment, it needs to be considered a crucial step of the development of the portfolio company. Therefore, the earlier four phases are extended to include an initial phase, called phase 0. This phase covers all the actions that are made prior to the acquisition of the company. All in all, five crucial phases have been identified as a part of the development of the portfolio companies, consisting of the phases: Phase 0-3 and the event based phase. The reasoning behind this grouping, and how to use each phase, will be discussed further below.

### 5.3.4 Selecting the Right Tools at the Right Time

All of these phases are based on the investors' development methodology. A methodology that differs to some extent since the business developers need to choose the right course of action and the right prioritization for each individual company. The phases should therefore only be seen as a schematic guide to their development process, where the steps in each phase requires extensive assessments and analysis to be developed in the best possible way. The requirements for such analysis will depend a lot on the company that is to be developed. Where factors such as its markets, industry, maturity level and size will have a strong impact on how the company is to be developed. Only after having studied the characteristics of the company carefully, can the company developed in the best possible way. It is therefore extremely important to adapt the process for each company, which is likely why the investors value the initial stages so highly, where the investors and board is able to learn more about the company. However, since the business developers and boards of the companies differ, the way in which the companies are developed will likely differ to some extent. The individual developers will likely focus on the areas in which they are the most experienced, why the development will be influenced by the skills and traits of the developers. This further explains the importance of finding the right set of people for the board and senior management, since that experience will need to be aligned with the needs of the company. Which in turn requires the composition of the development team to cover the different improvement areas identified in the development process.

Therefore, it is not surprising that the investment company value the experience of their developers highly, whom all have previous management experience from larger industrial companies. Since their experience forms the basis when evaluating and implementing the different actions made in each company, one critical task for the investors is to attract and retain competent business developers. The investors attracted these individuals using a combination of personal relations and their contact with experienced managers from surrounding businesses. People they can ensure have proven themselves, through their actions when developing other companies.

Furthermore, the identified process depends highly on the investment strategy and practice of the investor. Why alterations to the process or the length of each phase may be needed by another type of investor, or an investor implementing another investment strategy. Where a shorter investment horizon for instance, will likely require an increased pace of development. Additionally, where other industries, that are not targeted by the investor, may require other actions as a part of the development.



## 5.4 Section 4: The Investors' Development Process

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This section will further analyze the identified phases that were identified during section 3, to form the identified development process used by the investors. This section will make the phases more tangible by describing the rationale for the grouping and the focus areas that, according to the development process, should be developed in each step.

### 5.4.1 Phase 0: Deciding to invest and Establishing Business Case

The phase is initiated when the investors decide to examine a potential investment, and ends with the decision to invest in the company.

#### 5.4.1.1 Rationale for the grouping

In section 5.3.3 the need for an additional phase was determined, a phase that covers the initial interactions between the investment company and the portfolio company. These interactions mainly consist of a number of different assessments, aimed at granting the investor further insights regarding the company that may be acquired. One of the most crucial steps of this assessment is the due diligence (DD), which consists of a number of different assessment areas. However, a comprehensive DD can be costly and time consuming, why many of the areas are often left out, or only investigated briefly.

The DD, together with any other assessments or analysis made by the investment company, is used to develop an initial strategy and business case for the company. Thereafter the company is acquired if the estimated profits exceed the expected price of the company plus a risk premium. All in all, the group focuses on the gathering of information and the establishment of an initial strategy used to make the investment decision, actions that are highly distinguished from the rest of the development.

#### 5.4.1.2 The actions needed

During the first step the potential company is assessed, and the decision to invest is reached. The reasoning for investing will not be discussed as a part of this section, since it is considered to be out of scope for the study. Instead, the focus lies with the developed business case and strategy, combined with the assessments made to learn about the company.

The extent of the work made during phase 0 will have a strong impact on the need for assessments during the following phases. Therefore, this phase urges the investor to perform a due diligence that is as extensive as possible. Where the cost of the assessments and DD, must be weighed against the potential return on investment and the need for further information. From the information gained, a business case and initial strategy for the acquisition needs to be made, where some fundamental components of the two are presented below.

### **Establishing a business case and strategy for the company**

This step should be seen both as the first and the final step before investing in the company. An initial investment and business case is formed to decide whether or not to go through with further assessments of the studied company or not. Thereafter further assessments and potentially a DD is performed, where all of the newly obtained information is used when finalizing the business case and the company's strategy. This forms the starting point of the following development and often consists many of the following goals and plans:

- Strategic goals
- Financial goals
- Potential Synergies
- Potential exit plan
- Acquisition targets

Note that "Acquisition targets" may include any following add-on acquisitions or acquisitions that made in parallel with the purchase of the studied company. If such acquisitions are made as a part of a larger deal.

**Gather insights from due diligence & assessments [note: level of depth may vary greatly]**

During this step the initial assessments are made, which can consist of both internal or external assessments in any special field determined to be of interest. Or it can be a fairly standard DD process, consisting of some of, or all of the most commonly studied areas in a DD. Some examples of such studied areas include:

- Financial assessment
- Overview of the areas: legal, taxes, contracts and compliance
- Market and sales assessment
- Vendor and supplier assessment
- Assessment of the organization and management, as well as any HRM related issues
- Technology, RnD and IPR assessment

**Make an investment decision**

As a last step, the overall assessments made are used to determine whether to acquire the company or not. Here the expected price of the company is compared to the predicted return on investment. However, since such activities have not been studied deeply, this will not be discussed further.

## 5.4.2 Phase I: Ready the Company for the Transformation

The phase starts after the end of phase 0, and lasts around four to eight months, depending on the maturity level of the company.

### 5.4.2.1 Rational for the grouping

The first activity-based phase consists of a number of different assessments and reviews that are initiated after the acquisition of the company. Most of these actions are either aimed at restructuring different parts of the company, or gather more information about the company, where the need for information is much based on the extent of the work made during Phase 0. Examples of such restructuring activities include the review and assessment of the: corporate structure, financing of the company, incentives, composition of the board and senior management.

All of these actions were performed during the first few months after the acquisition, combined with any actions that were a part of the original business, such as the planned acquisitions in Chem.Corp. Which distinguishes the group as an initial restructuring and assessment phase, aimed at readying the company for its upcoming transformation.

### 5.4.2.2 The actions needed

Phase 1 forms the starting point of the development, and is characterized by an initial restructuring of the company, and further assessments and reviews of the company. The length of this phase much depends on the maturity and stability of the company. Where a turnaround company may force the developers to act quicker than in a more stable company.

Initially, the company is restructured and potentially refinanced, so that the new structure best suits the investors. Furthermore, any potential add-on or follow-up acquisitions that were a part of the initial business case are implemented. Thereafter the board is reshaped to include new business developers from the investment company.

During this phase, the board and investors are to learn more about the company. Where the additional knowledge gained about the company is to be used when refining its strategy, and identifying the company's challenges for reaching its long-term strategy. These challenges are to be translated into a development plan, a plan that will guide the development made during the second phase. This plan is to be focused on any operational changes that are

needed before implementing the company's long-term strategy. Where other actions more focused on "trimming" an already functioning organization is to be excluded in these initial phases, to ensure that the company focuses on the most urgent issues at hand.

#### **Launch initially planned projects**

- Such as planned Acquisitions, or other actions that are a part of the business case

#### **Assess and develop corporate structure**

- The company's structure is redefined to best suit the corporate parent
  - Potentially leading to a restructuring of the company's structure, for example through the establishment of new holding companies
- Potentially refinancing the company
  - A 50-50 equity debt financing structure is preferred by the studied investment company
- Ensure initial compliance, e.g. according to the Swedish law: "Aktiebolagslagen"

#### **Assess and develop board**

- Assess the current board, with an additional focus on the chairman of the board
- Restructure the board based on the assessment and the need to include new owners' perspective or external board members
  - The new board's composition should grant the company access to the competence needed for the upcoming transformation
- Reshape the board's agenda and practices if needed
- Include any external board members in incentive programs

#### **Assess and develop senior management and organization**

- Assess the senior management team, with an additional focus on the CEO
- Make corresponding changes based on the assessment of the senior management, may include changes to the structure of the organization or the senior management team
- Implement incentive programs for the CEO and senior management, that are connected with newly set KPI:s matching the company's long-term strategy

#### **Gain deeper knowledge about company**

- Investors and business developers are to learn more about the company through their increased insights into the company and through the board

- Some sources of information include: the newly revised reports from the company, and external or internal assessments and studies

**Re-assess strategy and form a development plan**

- Refined and develop the company's strategy based on new assessment of the company and its surroundings
- Assess the company's readiness for implementing the updated strategy
  - Use this assessment to identify challenges and areas that are in need of improvement
- Translate the identified improvement areas into a development plan, where the change initiatives that are needed for readying the company are detailed
- Thereafter prioritize the activities needed, based on their long-term impact and ease of implementation

**Determine the urgency for change**

- Assess the urgency for change, where this initial learning phase can be allowed to be longer in a case with less urgency for change
- Thereafter decide when to start developing the operational aspects of the company, thereby initiating the next phase

### 5.4.3 Phase 2: Readjust to prepare for the Long-term Strategy

The phase starts after phase 1 and ends after two or three years, depending on the maturity of the company.

#### 5.4.3.1 Rational for the grouping

After Phase 1, the board and business developers have gained increased knowledge about the company, that is used for the continued development of the company. The actions included in this phase were mostly focused on the most critical improvement areas of the value chain, the senior management, sales and the overall growth of the company. Where the goal appears to have been to reach a “good-enough” level of readiness across the value chain, so that the company were to be ready to implement its long-term strategy. Other more strategical efforts, aimed at trimming the companies’ overall efficiency was mostly held off until the next phase.

Furthermore, some administrative and structural changes were made in this phase as well. Specifically, in the two smaller companies where these changes were put on hold in order to prioritize on other issues. This proves the need for flexibility, where this phase covers all actions needed to readjust the company, where other more strategical issues were dealt with in the next stage.

#### 5.4.3.2 The actions needed

Development stage 1 ends after having developed a re-assessed strategy and development plan, a plan that is used when determining what activities are needed in phase 2. These activities are to focus on the adjustment of the operational and organizational aspects that are needed to pursue the company’s long-term strategy. Such activities will therefore focus on the adjustment of preexisting areas at the company. The improvement of these areas depend highly on their current state, why the need for change will vary greatly. Therefore, a number of focus areas that may be in need of development are presented in the list below. The goal for this phase should be to develop these areas so that they reach a sufficient level. A level that is “good enough”, thereby enabling the company to reach its long-term strategy.

Additionally, one of the key objectives for this phase is to establish a strong organization and senior management, improve the company’s sales practices and evaluate new growth options. Why activities aimed at these areas are to be prioritized.

### **Organizational structure [the board of directors]**

- Does the board have access to the necessary capabilities required for the current and future needs of the company, given the re-assessed strategy?
- Does the board's routines and agenda meet the company's current and future needs?
- Do the reporting systems and routines allow the board to monitor the company in a sufficient way?

### **Organizational structure [Senior management]**

- Is the structure of the organization optimal given the long-term strategy?
- Is the current senior management capable of implementing the strategy?
- Is the CEO capable of leading or reshaping the senior management?

### **Financial and structural review**

- Is the financial structure best shaped for the current organization? Does the financing rely too heavily on debt or equity when compared to the investor's practice?
- Does the company have access to enough capital for the continued growth journey?
- Are changes needed to ensure compliance? E.g. transfer pricing

### **Growth assessment, best options are pursued**

The following growth options are assessed, where the best possible options are to be targeted for development. Thereafter the organization is assessed and developed to determine that it is capable of pursuing the chosen option

- Organic growth in current markets
- Organic growth in new markets
- Acquisition-based growth horizontally
- Acquisition-based growth vertically

### **Sales strategy and structure**

- Are there any new segments that the company should expand into?
- Is the company's segmentation best suited for its current and future situation?
- Is the company's salesforce best structured for the new segmentation?
- Is the company's pricing model best suited for the opportunities in the market?
  - Can the pricing model be redesigned to better resemble a value-based model?



### **Functional assessment [Operational]**

Initially, the primary activities in the value chain are targeted for development, to ensure the immediate operational efficiency of the company. These development activities are primarily to focus on operational improvements, strategical improvements are initiated in phase 3.

- Operations
  - Do the logistical and manufacturing activities reach a sufficient standard, across business units and products groups?
  - Does the profitability of any specific areas or products need to be developed?
  - Are there any other areas that are in urgent need of improvement?
- Resource and development
  - Is the RnD department focusing on the most value-adding activities?
  - Are new practices or initiatives needed, either internal or external?
  - Are there any acquisition targets that can help accelerate the product development in a cost and capability efficient way?
- Sales and marketing
  - Is the salesforce well-equipped to sell the company's products/services?
  - Are the number of sales representatives sufficient?
- Human resources
  - Is there a positive corporate culture in the company?
  - Are initiatives needed to develop/enforce the culture?
  - Are sufficient incentive programs in place, promoting a pay-for-performance culture?
- Economy/finance
  - Does the company have sufficient reporting structures in place?

## 5.4.4 Phase 3: Pursue the Strategy and Increase Efficiency

The phase starts after phase 2 and continues thereafter until a new process or phase is initiated.

### 5.4.4.1 Rational for the grouping

The actions that were implemented in the later stages of the development appear to have a much more strategic focus. These actions either focused on the implementation of the long-term strategy, or on the focus areas: growth options, operational efficiency improvements, a revised functional strategy and an increased organizational stability through succession planning. Some of the actions made show resemblance to the actions made in the second phase, though with a more long-term adaptation, where the previous goal of reaching a “good-enough level” is exchanged with the desire to trim the organization. This indicates a clear distinction between the two phases.

### 5.4.4.2 The actions needed

Phase 3’s core focus lies on the implementation of the long-term strategy and begins when the company has developed the areas that were in need of improvement. The development made highly depend on the defined and revised strategy, why the actions made will need to vary based on the specific characteristics of the company. One crucial part of the strategy should be an elaborate growth plan, why the company’s growth options are to be developed extensively. Specifically, through the evaluation of new market and product opportunities, either through building on newly launched ventures, or through entirely new ones.

Additionally, the operational efficiency is revised during this phase, where the functional strategical is revised with the purpose of increasing the performance of the company’s different departments. Especially the sourcing and operation practices are to be revised, where dual sourcing, lean and other functional strategies may lead to great efficiency improvements. Some of the most crucial areas regarding the strategy and operational improvement will be presented below.

### **Focus on the development and implementation of the long-term strategy**

The board’s and senior management team’s key focus should be on developing and implementing the strategy. Hence their focus should be on the most critical and strategically important areas. The following areas are to

be continuously developed by the other parts of the organization and with the help of the board after having initiated the strategical development.

### **Develop new and previous growth options further**

The previously selected growth option is developed further, where the other options are re-assessed based on the newly strengthened company's new capabilities. Regardless the focus should still be on the option/options chosen in phase two.

- Organic current markets
- Organic new markets
- Acquisition-based growth horizontally
- Acquisition-based growth vertically

### **Adapt the product portfolio in line with strategy**

The product portfolio is to be extended or revised to best match the long-term strategy. This may require different sorts of actions, such as organically growing the portfolio through external or internal RnD, extending it through M&A or divesting unwanted product groups

### **Functional assessment [strategical]**

The review and development of the functional aspects of the company is continued in phase 3. Though the focus is to shift from operational to strategical activities, such as reviewing the sourcing strategy and long term HRM plan. Some more detailed aspects are presented below.

- Operations and procurement
  - Ensure the fundamental efficiency of the operations
  - Review the functional strategy for the operations and procurement. Where more developed strategies in the areas: sourcing, supply chain management or manufacturing may lead to significant improvement
- Refocus the RnD department so it best serves the long-term strategy
- Sales and marketing
  - Ensure the capacity and efficiency of the Salesforce, improve if necessary
  - Ensure that the segmentation best capture the long-term strategy
  - Ensure that the sales activities are best aligned with the selected growth options developed by the company
- Human resources
  - Ensure the present and future strength of the organization by implementing succession programs and talent management

- Further develop the culture of the company and ensure that it promote taking initiatives and responsibility for the employees' actions
- Economy/finance
  - Ensure the company's financing structure and access to capital
  - Continue the development of reporting systems, proactively readying them for the changes that are, and will be made
- Legal
  - Continuous assessment of company's surroundings, ensuring legal compliance and integrity of IP-rights and marketing practices

## 5.4.5 Phase X: Readjust due to Radical Change

The phase is initiated after having identified a crisis, and lasts for the duration of the crisis.

### 5.4.5.1 Rational for the grouping

In the second stage of the analysis section, the need for an event-based group was determined, since not all actions should be seen as a natural part of a development process. These actions include specific legal actions and crisis readying actions, caused by dramatic change in the internal or external environment. These actions are clearly distinguished from the others, since they do not seem to follow a specific development pattern, but instead relate to the current situation of the company.

### 5.4.5.2 The actions needed

The final development phase covers crisis management, as a response to a radical change in the internal or external environment. The crisis management needs to be developed based on the situation at hand. Nevertheless, there are still three steps that should be seen as a crucial part in all crisis management. A proactive monitoring of the companies should be seen as the first step, since the monitoring allowed the developers to act quickly. Thereafter the situation in all of the companies were evaluated extensively, to better understand the situation and its possible outcomes. Ultimately, a detailed plan was developed in all of the cases, which was preferably to be modular, allowing them to act in different ways depending on the outcome of the situation.

All of these actions require a lot of time and resources from the board and investors, though tackling a crisis without a developed plan will likely be more troublesome, and risk leading to more severe negative consequences for the company. The identified three steps are discussed further below.

### **Use developed reporting channels to proactively scan for emerging crisis**

The board and investors are to monitor the company frequently, regardless of the situation of the company. When it is performing well, the actions needed are fewer, though the need for close follow-up remains. Some of the key areas that are to be monitored are: order intake & backlog, communication with suppliers and customers, information regarding the performance of senior management and any critical events that the company is facing. This information is to be assessed by the senior management and board continuously, to early identify any potential issues or crisis.

**When crisis is identified: assess the situation to gather information**

Senior management, external consultants or operationally active board members help gather the information needed to analyze and evaluate the situation. Predictions are made to establish a sense of understanding of the situation. Scenario planning and analysis is preferably used, to identify different outcomes of the situation.

**Develop modular countermeasures based on scenario analysis**

A detailed is to be developed, preferably based on the scenario analysis made in the previous step. The plan is best made in a modular way, to increase the company's flexibility and allow them to respond at different levels, depending on the outcome of the situation. The countermeasures should be combined with increased levels of involvement from the board and senior management. Where the board should preferably work alongside the organization when tackling crisis. If suitable, the rest of the organization is to be informed continuously, to unite the organization when resolving the crisis.

## 6 CONCLUSION

The most central finding of this study is the process through which the investment company develops its portfolio companies. A process that despite its need to be flexible still resemble a clear generic process which can guide the development of different types of companies. The process shows the importance of first gathering information and knowledge about the company through the due diligence and an initial learning stage. Which is then used to ready the company for its long-term success. Hence, the initial development is focused on the core aspects of the company, with a certain focus on strengthening the organization and senior management. Only after having established a strong central organization should the focus shift towards growth and efficiency improvements. These final improvements are the ones that are to increase the value of the company the most, and pose the core of the long-term strategy that forms the basis for acquiring the company. However, since the companies are to be held for a long time it is first important to equip them with the tools and capabilities needed for reaching their long-term goals.

The process differs based on the company that is to be developed, since several aspects will influence the company's need for development. Some of these aspects include: the characteristics of the company, what industry it operates in, what markets it serves and how mature or stable the company is. One of the key challenges when developing a company is to identify these differences and to adapt the process to best suit the specific company. The main areas of the process will remain the same, though the prioritization and the tools needed will vary between companies.

Two areas that allow the process to be flexible is the content and the length of each phase, which can be adjusted for the needs of the company. This flexibility requires the developers to quickly determine when and how to act, why the timing of each action and length of each phase is very important. Such flexibility requires the developers and the board to quickly learn about the company. Therefore, the initial stages have a clear focus on learning more about the company, insights that are to be used when determining what actions to initiate and how to refine the long-term strategy. Furthermore, the flexibility puts further requirements on the composition of the board and the senior management. Where the knowledge gained regarding the company must be used to ensure that the composition of the board is best suited for the current and future needs of the company.

When studying the following development process, one must keep in mind that this process has been designed by an investor with very specific characteristics. These are fairly similar to other private investors, though when comparing them to commercial investors, it is clear that their generally longer investment horizon will cause them to develop companies differently. This difference can allow them to be less aggressive than an investor seeking to divest the company within a few years. Therefore, the process should be expected to have a larger focus on the strengthening of the company's long-term capabilities, with little regard to financial engineering or other activities that increase the value of the company in the short-term. This likely explains the investors strong focus on the development of the senior management and organization of the company, where a commercial investor may instead rely more heavily on consultants or similar actors. The comparison between private and commercial investors have not been the focus of this report, though studying the area further would likely reveal many more interesting differences or similarities. Regardless, these differences must be kept in mind before using the process in a context that differs much from the studied investor.



## 6.1 The studied investor's development process

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The development process of the studied investment company can be summarized with the following illustration, which highlights the most important development areas for each development phase. The phases 0-3 are centered around the first 5 years of a company's development and transformation. Phase X focuses on the crisis management needed when responding to drastic changes in the company's environment.

(Note, the following illustration is only a summary of the finding presented in the analysis' section 4, why a reader wanting to focus on the conclusion is advised to read that specific section as well.)

Phase	Actions and Focus Areas
<p style="text-align: center; font-size: 48px;">0</p> <p style="text-align: center;">Time until acquisition</p>	<p>Deciding to Invest and Establishing Business Case</p> <ul style="list-style-type: none"> <li>• Establishing a business case and strategy for the company</li> <li>• Gather insights from due diligence &amp; assessments</li> <li>• Make an investment decision</li> </ul>
<p style="text-align: center; font-size: 48px;">1</p> <p style="text-align: center;">Day 1 – Month 4-8</p>	<p>Ready the Company for the Transformation</p> <ul style="list-style-type: none"> <li>• Launch initially planned projects</li> <li>• Assess and develop corporate structure and board</li> <li>• Assess and develop senior management and organization</li> <li>• Gain deeper knowledge about company</li> <li>• Re-assess strategy and form a development plan</li> <li>• Determine the urgency for change</li> </ul>
<p style="text-align: center; font-size: 48px;">2</p> <p style="text-align: center;">Phase 1 – Year 2-3</p>	<p>Readjust to prepare for the Long-term Strategy <i>(Focus development on the areas below that are expected to have the highest impact)</i></p> <ul style="list-style-type: none"> <li>• Organizational structure [the board &amp; Senior management]</li> <li>• Financial and structural review</li> <li>• Growth assessment, best options are pursued</li> <li>• Sales strategy and structure</li> <li>• Functional assessment [Operational]</li> </ul>
<p style="text-align: center; font-size: 48px;">3</p> <p style="text-align: center;">Phase 2 - Onward</p>	<p>Pursue the Strategy and Increase Efficiency</p> <ul style="list-style-type: none"> <li>• Focus on the development and implementation of the long-term strategy</li> <li>• Develop the new and previous growth options further</li> <li>• Adapt the product portfolio in line with strategy</li> <li>• Functional assessment [strategical]</li> </ul>
<p style="text-align: center; font-size: 48px;">X</p> <p style="text-align: center;">During a crisis</p>	<p>Readjust due to Radical Change</p> <ul style="list-style-type: none"> <li>• Use developed reporting channels to proactively scan for emerging crisis</li> <li>• When crisis is identified: assess the situation to gather information</li> <li>• Develop modular countermeasures based on scenario analysis</li> </ul>

Figure 25: The investment company's development process

## 6.2 Validity and Reliability

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In this report only one private investment company has been studied, which risk limiting the generalizability of the results. Specifically, this means that the compiled development process can only be expected to reflect the specific investor. Regardless, the finding should be seen as fairly generic, why the process can still be used either as a guideline for developing companies, or to understand the specific investor or private investors in general.

Furthermore, only some of the investor's portfolio companies were selected. These companies were selected based on a number of different criteria that can be found in the methodology section of this report. These aspects were used to ensure the similarity of the portfolio companies, which simplify the comparison of the companies when identifying the development stage. However, this risk limiting the result since other types of companies may have contributed with other types of actions or timing. Regardless, the selected companies are still different from each other, in terms of industry, size and maturity level. Why the lacking number of portfolio companies should not be considered to have a significantly negative impact on the result.

The lion share of the empirical data is based on interviews and observations, information that due to their subjective nature risk being misinterpreted. The risk lies both in the interpretation made by the author, where the claims made during the interviews or during the observations risk being misinterpreted. The other risk lies with the interviewees interpretation of the historic events, which could potentially be misleading. However, a lot of efforts has been made to reduce both of these risks. The external conferences and seminars attended by the author has allowed for a broader understanding of the subject, which reduce the risk of the author misinterpreting information. Additionally, the combination of multiple interviews from different parts of the organization, observations and archive analysis should reduce the data's reliance on subjective information.

Another risk connected with the interviews is the risk of them not digging deep enough into the subject, thereby risking to miss important aspects of the development. The outcome would then be that the data fails to reveal the "how" of the development, resulting in a shallower outcome. This too is counteracted by the width of the study, why it is not determined to have a significant effect on the study.

Ultimately, since the material was forced to be masked, some critical information risk being left out. This allowed the author to get access to confidential information such as the board minutes, which granted the author better knowledge about the company, likely leading to a better result. However, this was done at the expense of the reader's ability to follow the results, which may rightfully cause the reader to feel that some information is left out. Regardless, this should in no regard have had a negative impact on the result.

### 6.3 Application and Usability

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The results of this report can be seen to have many different uses. Some of these are directly connected with the compiled development process, where others may instead find the work processes in the portfolio companies to be more interesting. Hence, the usage depends on the interest of the reader, where many different actors can be expected to gain from this report. Some examples of such actors include: the investment company itself, other investors, company's seeking to improve their development processes, or a student or scholar wanting to learn more about the topic. Some different usages for these groups are presented below.

The studied investment company may use the process when benchmarking the actions made in the studied companies to that of the other companies. This could be done to share experiences within the company and to further analyze the actions that were made in each company. Where such knowledge sharing might help the developers to broaden their skills and experiences when developing new ventures or investments.

The development process and the actions made can further be used when comparing the investment company to other types of investors, private, commercial and strategic alike. The similarities and differences that are identified can be used to either develop a deeper understanding of the different investment groups, or for any of the groups to learn from the others. Such information can also be used by an external party researching any of the different investment groups individually, or as a broader group.

Other types of companies may also use the process to draw insights regarding business development from a broader perspective. Such companies could include other types of industrial investors, private companies, or external actors and consultants. However, a lot of these companies will likely not have access to the same resources as those of the studied investment company.

Where their limited resources may hinder them from getting access to the competence needed for implementing such a flexible development process. Nevertheless, such organizations may instead acquire such competence through the recruitment of senior external board members. Where many competent external board members can be recruited at a reasonable price, especially in the cases where such a board member may have personal reasons for supporting the company.

## 6.4 Further Research

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There are several different areas that can be researched using this thesis as a foundation. One such area that could be investigated would be to research more private investment companies, can be studied, to investigate similarities or differences among private investors. Such assessment can be used to investigating the generalizability of the results from this study, as well as to strengthen or improve the identified process through the usage of more empirical data.

Additionally, each development phase and its content can be investigated further, to grant deeper insights to *how* the actions are to be shaped and a better understanding of when to act. Such an investigation could thereafter be used to identify any similarities and differences regarding the the content of each phase.

Furthermore, a comparison between private and commercial private equity investors can be made. Here the comparison of the development processes and actions for each group can be assessed to find any differences in their development methodology. This methodology will depend a lot on the characteristics of the investor, regardless, these differences can potentially be used to gather deeper knowledge regarding the actions that can be made. Which can be used to shed some light on how the processes are adjusted for each studied company, where best practices can likely be identified and used in further development.

The findings in this report could further be used with other assessments to fill the research gap that exists for private investors. This could in a next step be used to investigate how private investors may influence the society in a broader context. Such as the studies that have been made for commercial investors as presented in the background to this report.

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