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DRIVING VALUE THROUGH AUTOMATING BORING, CUSTOM TASKS

Private Equity Value Creation Series

With increasing EV/EBITDA multiples amid a space overflowing with equity capital, successful private equity firms (PEs) are shifting towards a model that emphasizes Value Creation. Some firms have split this function out, analogous to the division between the “Business Development” and “Investment” Teams, with names of these teams including “Portfolio Management”, “Value” or “Value Creation”, “Portfolio Support” or (as a subsidiary function) “Data Science.” In the midmarket (<\$5B of assets under management), resources are scarcer, so firms are looking to add value inexpensively and creatively. Sapling Financial Consultants Inc. (“Sapling”) assists a number of private equity firms with various aspects of Value Creation on the Finance side. This is one of a series of whitepapers covering how midmarket PEs can Drive Value in portfolio companies through optimization of the Finance function.



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One of the things we see PEs do successfully on a consistent basis is enhance financial reporting, and to a lesser extent operational reporting (KPIs, dashboards, etc.). Good reporting is foundational to adding value to portfolio companies. After all, what is not measured cannot be easily improved. However, reporting’s impact is long-term and strategic in nature, with the \$ of value created measured over longer periods of time and with lesser degrees of certitude.

An area of Value Creation that bucks this trend is the automation of repetitive tasks, or “Finance Automation.” By “Finance Automation”, we mean the reduction of labour time through the use of software or software tools. With Finance Automation, we can easily calculate \$ in/invested (one-time staff time and consultant time, and one-time/ongoing software costs), and \$ out/saved (reduction in staff time on an ongoing basis), and thus ROI, NPV, IRR, etc. The issue is that Finance Automation is already to some extent baked into even the most poorly-run (potential) portfolio companies. A lagging company 20 years ago may have had paper ledgers, but today they use QuickBooks or Sage to invoice semi-automatically, track AP, and so on.

As a result, the low-hanging fruit of moving to a new Finance system has already passed most PEs by. The idea that you can drive \$1M of new EBITDA per year through migrating to NetSuite or Great Plains could actually be dangerous since much of that value is already built into the EBITDA you purchased at now-elevated multiples. Software packages like



QuickBooks and others became prevalent precisely because they quickly added value to typical tasks. Where they fall short is with tasks that are not typical.

Consequently, some of the highest benefit-to-cost tasks to automate are those that are truly customized. Take, for instance, a health care portfolio company whose AR team has to take time entries from their in-the-field therapists, and then manually type out each entry into an insurer's web portal in order to get payment some 30-60 days later. Or think of the firm that has 5 different in-house commission structures and 10 (and growing) referral fee structures, and which has to generate monthly statements as well as a cheque to salespeople and referral partners.

The typical solution – especially at owner-managed businesses – has been to throw bodies at the problem. But it's easy to make mistakes with boring, repetitive tasks, and

moreover, finding the right people, who are reliable and want to do such work long-term, is uniquely difficult. In fact, we work with numerous bookkeeping firms that cover this type of function, and every single one of them has been in constant labour shortage mode for years, largely because people (quite reasonably) want to do interesting work. So fighting turnover and trying to over-resource the hiring/human resources function is a corollary of this increasingly-losing strategy.

"Enterprises" tend to be well-served by an ecosystem of "Robotic Process Automation" ("RPA") products like UiPath and Blue Prism, and implementation firms including the Big Four, Accenture, IBM and others, but these projects typically run into the hundreds of thousands of \$ once software and implementation services are included. In short, they are not accessible to the midmarket, and not accessible to midmarket PEs.

Smaller companies, where they are able to execute in these situations, tend to leverage a single “star” employee, whose abilities far outshine the job description and who undertake value-adding, high-complexity initiatives eagerly. Where such an employee is available, certainly they should be used in such a manner! But finding the skill set and inclination to repeatedly do this, especially across numerous portfolio companies, is difficult to do systematically.

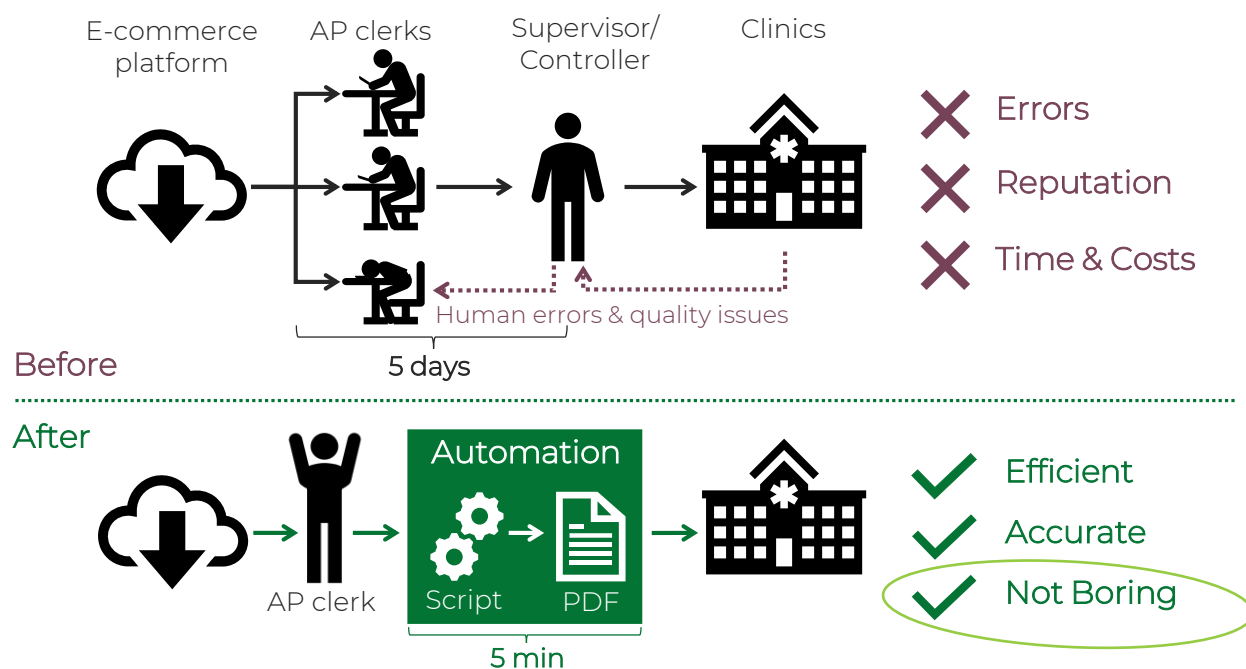
The boutique, non-enterprise solution involves leveraging more affordable packages, custom programming (Python, VBA, SQL), Excel, and free web scraping libraries to fit many different automation situations on a “shoe string”. Since an entire system is not being implemented, the consultant hours to develop it stay reasonable, and the software costs remain limited.

One **technology** company has a patchwork of systems that generate billing data, with several systems (some legacy) for each service, of which there are a number. To generate a bill in

their cloud-based invoicing system, their existing process was to use a large team of AR clerks who took the data, made numerous manual modifications in Excel and Word, and then “fat fingered” the data into their invoicing system. This was done for each and every customer, of which there are thousands, every single month. The “shoe string” solution they selected involves an automated download of data using desktop-based “web scraping” scripts, formatting and manipulating the data in Excel, and then automated “form filling” mimicking a human user in the cloud-based invoicing system. There are, of course, numerous areas where human intervention is necessary, and the process that was developed is tailor-fit to this reality. Estimated time savings reached 60% each month.

Another company in the **healthcare** space pays commissions to clinics based on the purchases of individuals that the clinics refer to the company. Each clinic has a different commission structure, with varying tiers, and bonuses based on achieving certain milestones. Each month, the company has to

Figure: Healthcare Example - Automatable Finance Process Before & After



produce a PDF statement, delivered to each clinic, detailing the revenues generated from the individuals that they referred, and the calculation of their commission payment. The selected solution was a database built in Excel, calculating all of the peculiarities of each commission agreement. The Finance team's only task each month is to download all of the transactions and purchasers from their e-commerce platform, paste them into two Excel sheets, and to click a button. The database then generates dozens of different PDF statements, each one detailing all relevant transactions and calculation methodologies for a specific clinic, with the payment owed at the bottom. Relative to their existing manual processes, savings were estimated at 80% of

the time associated with this task.

To conclude, the business case for automating boring, custom tasks is straightforward. PEs that can afford enterprise-quality systems should avail themselves of the opportunity, while those that have a "star" employee at portfolio companies that can implement solutions should leverage that person and keep them incentivized and motivated. For those firms that are lacking such options, engagement with a financial consulting boutique with experience leveraging affordable packages and custom programming is a reasonable and cost-effective way forward.



