Generating Returns: Can Private Equity Help Your Standby Power Business?

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Private equity has become more prominent in the standby power industry with companies such as GenServe, GAL Power, Central Power and National Power all partnering with private equity firms in recent years. For even the most seasoned entrepreneurs, discussions with private equity firms can be complex and unfamiliar - touching on topics like valuation, capital requirements and succession planning. Often, entrepreneurs will ask themselves numerous questions after being contacted by a private equity firm, including: what is private equity, what type of private equity firm fits my needs, and what does partnering with a private equity firm actually mean for my business? Our goal in this article is to demystify private equity and highlight the questions you should ask yourself if you decide to engage with or learn more about private equity.

What is private equity and why would I partner with a firm? Private equity is a segment of the investment industry whereby firms make equity investments primarily in private businesses. Typically, private equity firms seek to make investments in growing businesses, with the intention of driving continued and accelerated growth to generate a return on their investment. These firms invest on behalf of a diverse group of investors including family offices, endowments and pension plans.

There are various reasons for businesses to partner with a private equity firm, including:

- Driving growth initiatives,
- Providing capital to fund strategic projects and acquisitions,
- Providing partial or full liquidity to shareholders to de-risk personal net worth,
- Strengthening the company's balance sheet, and
- Assisting with ownership transitions for passive shareholders or succession plans from one generation of entrepreneurs to the next.

Under what terms can I expect a private equity firm to invest? Private equity firms each have their own style of investing; but in the simplest terms, this can be in the form of a majority investment (also known as a "buyout") or minority partnership. With a majority investment, the existing shareholders give up operating control of the business to the private equity firm, who would control the business going forward. This option could be attractive to entrepreneurs who are looking to step back from the business and receive significant or full liquidity. In minority partnerships, the existing shareholders retain control of the business and the private equity firm invests alongside the existing shareholders to help accelerate its growth and strategic value, which may eventually lead to a more lucrative sale for all parties in the future. With this structure, the existing team continues to benefit from further upside in the business and may still receive partial liquidity, depending on the situation.

In both majority and minority transactions, it is important to understand the difference between ownership and rights. Even in the case of a minority partnership, the private equity investor will have governance rights such as board representation, budget approvals, and liquidity or drag rights after a certain number of years. Discussing these rights clearly at the outset is a must to foster a successful partnership.

How will I operate differently when I partner with a private equity firm? Every private equity firm will have a different approach to provide ongoing support for the business. Some firms provide capital and have limited involvement with the business on a go-forward basis (i.e., only engaging around and attending quarterly board meetings). Others work more closely with management, supporting initiatives like acquisitions and major capital expenditure projects. In our experience, businesses typically benefit from a partnership-focused private equity firm in the following ways:

- Supporting acquisitions, including identification of targets, negotiations, due diligence, and closing/integration plans,
- Building strong corporate governance practices, including bringing on independent board members, changing the corporate structure and implementing critical policies,
- Hiring key management personnel to further strengthen the organization, including finance, operations, marketing, and sales, and
- Accessing better and cheaper financing, (i.e., leveraging the private equity firm's network of lender relationships).

What does the process look like for working with a private equity firm? The process begins with initial negotiation of the key transaction terms: the valuation of the business, percentage of ownership being sold (majority or minority), future involvement of existing owners/management and key rights post-close. Once this is completed, a letter of intent (LOI) would be executed by both parties and due diligence would commence. During this period, the private equity firm would analyze several aspects of the business including financials, operations, and management to better understand the business and begin planning for its future.

Once the due diligence process is complete, the existing owners would enter into a sale and purchase agreement as well as a shareholder agreement which together define the terms of the sale and revised rights of all owners. Once all the agreements are signed, the transaction would close, and the new ownership would be in effect. Afterwards, the private equity firm and management would work together on implementing the growth strategy of the business, including how to take advantage of opportunities such as acquisitions, winning new customers or forming strategic relationships.

What does this mean for my business? The market for standby power is continuously evolving, and with these changes, business owners will increasingly need to explore alternatives to support their business. In the event you wish to receive full or near-full liquidity and step away from the business, selling to a buyout firm or a competitor could be an appropriate option. In this scenario, the entrepreneurs and existing shareholders should consider the following: am I receiving full value for the business, what is the plan for existing employees under new ownership and will the new owners continue to uphold the brand and reputation that was built? Other the other hand, if you wish to continue driving the business and see value in its future but would like a partner to help capitalize on opportunities, pursuing a minority partnership with a private equity firm could be the best choice. In this situation, entrepreneurs and existing shareholders should consider the following questions: how will this private equity firm help drive value, what does a partnership look like with this firm, who would be involved and how would important decisions be made after the investment?

In the end, there is no right answer, but given the growth of private equity in the standby power sector, it is important to understand if private equity is right for you, and if not, how it may be impacting others – including your competitors. If you choose to engage with a private equity firm, understand your needs and alternatives beforehand and diligence the firm with whom you are communicating.

If you decide to engage with a private equity firm, we encourage you to take the time to learn about the firm before jumping into a transaction and we are happy to answer any questions you may have on the sector! ●

About the Authors

Mohit Kansal and Austin Sinclair are investment professionals at Clairvest Group (www.clairvest.com), members of EGSA and are attending the EGSA fall conference in San Antonio. Clairvest is a private equity firm based in Toronto, Canada that has been partnering with entrepreneurs to build strategically significant businesses for over 36 years. Clairvest is actively seeking opportunities to partner with businesses that have more than $5M of EBITDA and will invest between $30M and $120M either in minority or majority transactions.