KEYNOTE INTERVIEW

Going global in the mid-market

The mid-market has proved a resilient place to be during covid-19, with geographical diversification a key upside, says Heather Faust, managing partner and co-founder of Argand Partners

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Q Argand focuses on investments in the global mid-market. What do you find attractive about that space?
We like to target advanced manufacturing and business services companies that are niche market leaders and help them grow into global champions in their sectors. Our team has deep experience with global mid-market companies having done this collectively for decades, and we love working with them on the whole process, across strategic repositioning and operational improvement, to help them reach their global growth goals.

For Argand, 'global' does not mean non-US; it means multiple co-ordinated international operations. We find there are very few global mid-market private equity sponsors. Generally, the truly global private equity firms are among the largest and focus on much bigger global deals.

A lot of these businesses tend to be under-resourced from the global perspective, just because of their size. One of the core tenets in building Argand was bringing together a group of individuals who were passionate about working with portfolio companies and helping them grow. We have developed a broad set of resources, covering finance, communications, marketing, legal and more, which we bring to each one of our businesses. These are mid-market businesses that we are able to support as they transition into larger global players.

In terms of what we find attractive, we see a lot of advantages in the resiliency global businesses have across market cycles. For example, several of our companies sell products in more than 100 countries. These types of businesses have a lot of diversification in their sales, and they tend to have global manufacturing footprints that bring flexibility on the operations side.

We can also work across different

geographies to bring best practice globally to these businesses. An interesting example of that was in the very early months of covid – starting in January 2020 – when one of our companies had facilities in China that allowed us to see emerging best practices for health and safety for employees in a pandemic and roll those out across our portfolio. We were also able to look at government directives in different geographies and shift production across a much broader footprint than we could have done with a company that was concentrated in its geographic supply chain.

Q What are the biggest challenges and opportunities that you currently face when it comes to value creation?

The biggest challenge for us of late is that we traditionally spend a lot of time on the road. We are very hands-on with our companies, visiting their locations around the world and working not only with their C-suite executives but also with management at their different locations. Obviously, covid forced us to rely on the technology we had fortunately built within those businesses for those communications, but it is not the same. We have started to travel again, domestically and internationally.

On the positive side, because we have been active in global markets for a long time, we have deep networks, not least through our Senior Executive Advisors, several of whom have been involved with our portfolio companies or businesses our team has invested in previously. That network, as well as our broad historical experience and relationships, means we are able to have people on the ground as needed even if we cannot be there directly.

Covid highlighted the value of having regular interaction with our management teams over time, and just being available and accessible whether in-person or remotely. That relationship we build with management is so important, because we have had to deal with a lot of tough but important topics over the past 18 months, like labour shortages and supply chain disruption. Without those well-established relationships, our ability to deal with those things remotely, when we couldn't sit across the table from each other, would have been compromised.

Another area we focus on for value creation is new product development and innovation. We are looking for ways to help companies grow, and the biggest challenges on the new product development front over the last year have been macro sourcing challenges, particularly in electronics. In some

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Q What trends are you currently seeing in the mid-market, and how are those impacting your portfolio?

The trends we see are consistent with broader trends everyone is talking about on a daily basis, including shipping costs and constraints, shortages in electronics and other components, raw material price increases and labour shortages. As we look at our global operations, we can more actively manage production and supply chains across locations, leaning in on global sourcing and shifting between geographies.

We think about investing both thematically and opportunistically, but a lot of the themes we watch and invest behind have global application. We like outdoor living; segments that relate to authentication, testing and supply chain verification; and climate change and sustainability, among others. We tap into these global themes and work to build niche market leaders into global champions, both organically and through strategic add-ons, looking for opportunities in various geographies.

An important part of our approach is that all our businesses have some sort of US nexus, which could be that they are headquartered in the US, they have significant US operations, or the US is an important growth market for them going forward.

cases, we have had to delay product launches by a year, which is unfortunate. There is still innovation we can do but there is going to be some pent-up demand on the innovation side when we start to see a better supply of chips.

Q How would you describe your investment approach?
The core of what we do is looking to take these advanced manufacturing and business services companies that are niche market leaders, companies that are very strong in their space, and helping them grow. For us, that means helping companies develop their strategic positioning and build the team and infrastructure to support both significant organic or acquisition growth on a global scale. We help structure our portfolio companies with the systems, the processes and the strategic focus to become global leaders in their categories.

Many of these businesses have some form of global operations when we acquire them, but they tend to be on the smaller side, so we help them to scale up. Typically, our businesses when we first invest are in the region of $20 million to $50 million EBITDA – we are looking for resilient business models, strong market positions, a sustainable competitive advantage and defensive characteristics that enable them to perform well across different economic environments. We are also looking for multiple levers for growth during the course of our ownership.

We want to create value through every step of the investment life cycle, including sourcing and execution. We are patient investors, so we take a disciplined approach to finding the right businesses at appropriate valuations, which is critical given the hands-on nature of our approach during ownership. To enable us to spend real time with each of our companies and support their growth, we take a more concentrated approach: a typical fund might have six to nine portfolio companies with potentially multiple add-ons for each company.

“The pandemic reinforced that... global businesses can weather various economic environments and there is value in global diversification”

Q How has your mid-market industrial sector strategy performed through the past 18 months? Have you made any changes to the strategy because of the disruption?
Our strategy played out the way we expected it to, and our companies proved resilient through the pandemic. If anything, the pandemic reinforced that core tenet of our thinking, that global businesses can weather various economic environments and there is value in global diversification.

This is a strategy the team has been investing in for many years, and, before forming Argand, we had a similar experience through the 2008-10 global financial crisis, where these types of global businesses performed well in a tough economy. We take a lot of comfort in that.

One of our portfolio companies, OASE, is a global provider of high-end water design systems and water technology solutions, headquartered in Germany, but with operations throughout Europe, the US and Asia and sales across 100 countries. That is a great example of a business that had solid underlying growth pre-covid and continued to fare well even during the pandemic. It responded and managed very flexibly across its global operations, and we used those lessons to roll out similar operational responses across our entire portfolio.

Q What is your outlook for next year, and where do you see investment opportunities going into 2022?
The market has been very busy this year, with 2021 activity at record levels. Everyone seems to be operating at capacity given the pent-up demand from last year, and we expect that to continue into 2022, perhaps slowing a little but remaining incredibly active.

We are optimistic about the year ahead. In terms of investment, what has been interesting is that companies are increasingly looking at ways to invest in automation and technology to enable more efficient production and service delivery. Many businesses have struggled to fill positions over the past year and so are focusing on maintaining production and service levels for customers even if labour is hard to come by, so that is one of the big themes we expect to see continue this year and next.

The demand for bringing in more automation trickles all the way through the supply chain, so lead times to get new machinery and some of this automation capability are being hit, with those companies experiencing their own production delays. That means this may be a process that extends over several years until companies finally bring in these intended improvements.

Lastly, ESG and diversity, equity and inclusion will continue to be tangible areas of focus, both in the types of investments private equity will make and also in the way firms drive change within each company in their portfolio and communicate that progress. This is another area where global experience can enable us to bring the best practices from different geographies to our portfolio. We are excited to see the momentum behind these efforts finally accelerating since we believe this will ultimately accrue to the benefit of all stakeholders. ■