Value Creation and Operating Roles (Private Equity)

Interview preparation summary · PE track

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INT.VO.1.a · Sources of value and operational levers

Build a value bridge that splits the growth in equity value into EBITDA growth (revenue and margin), change in the multiple and deleveraging, and explain why multiple expansion is not a plan.

A value bridge explains how the equity value of a portfolio company moved between entry and exit. The usual sources are EBITDA growth, change in the valuation multiple, and the reduction in net debt from cash generation. With a stated convention they add up exactly: EBITDA growth valued at the entry multiple, plus the change in multiple applied to exit EBITDA, plus the fall in net debt, equals the gain in equity value (before fees and any dividends). EBITDA growth can be split further into revenue growth, valued at the entry margin and entry multiple, and margin change, applied to exit revenue. Say which convention you use, because a different order moves a small cross term between the lines. Deleveraging is not a separate skill: it is paid for by cash that the business generates, so it depends on EBITDA, capital spending, working capital, interest and tax, and it can be negative if acquisitions are funded with debt. Multiple expansion is the weakest source because the exit multiple is set by the buyers and the market at the time of sale, not by the owner, so a sound plan underwrites an exit at or below the entry multiple and treats any re-rating as upside. Interview point: show the bridge reconciles and say how much of the return the team controls.

WORKED EXAMPLE: BRIDGING A 213 GAIN IN EQUITY VALUE

A fund buys a company with revenue of 200 and an EBITDA margin of 15% at 8.0x EBITDA, with net debt of 120. Five years later revenue is 280 at an 18% margin, the exit multiple is 8.0x and net debt is 70. Ignoring fees and dividends, build the value bridge, and show what happens if the exit multiple is 7.0x.

Answer: The 213.2 gain is 96.0 from revenue growth, 67.2 from margin, 0 from the multiple and 50.0 from deleveraging. At a 7.0x exit the gain falls to 162.8.

> **Interview tip:** State your convention, show that the lines add up to the gain, and say that you would underwrite the plan on a flat multiple and treat any re-rating as upside.

INT.VO.1.b · Sources of value and operational levers

Size the main operational levers (pricing, procurement and cost-out, working capital, footprint, SG&A, and digital and AI-enabled efficiency) with their one-off costs, payback and effect on margin.

Operating partners are expected to size levers in numbers. Pricing usually has the fastest and largest effect because a price rise falls almost entirely to profit if volumes hold, so test it against the volume that can be lost before the gain disappears: with a price rise p and a contribution margin c on the old price, that break-even volume loss is p divided by (c plus p). Procurement savings apply to addressable spend, not total spend, because rent, taxes and regulated items cannot be renegotiated, so multiply the addressable spend by a realistic percentage and set it against the one-off cost to achieve. Working capital release is a one-off cash inflow, measured in days of sales or cost, that reduces debt but does not raise EBITDA or add to enterprise value. Footprint and capacity moves save fixed cost but need capacity checks, closure costs and a plan for customers. SG&A savings come mostly from people and need redundancy costs. Digital and AI efficiencies count only when hours saved become removed cost or redeployed revenue capacity, backed by a pilot, an owner and measured adoption. Run-rate savings are not in-year savings: phase them and deduct one-off costs. Interview point: give a number, a payback and the main risk for each lever.

WORKED EXAMPLE: SIZING A PROCUREMENT AND WORKING CAPITAL PLAN

A company has revenue of 150, EBITDA of 24 and third-party spend of 70, of which 50 is addressable. Management expects to save 6% on addressable spend, with one-off costs of 2.0. Separately, it will cut receivable days from 60 to 52. Size the EBITDA and margin effect, the payback, and the cash release.

Answer: Procurement adds 3.0 of annual EBITDA (margin 16.0% to 18.0%) with a payback of about 8 months, and the receivables plan releases about 3.3 of cash once.

> **Interview tip:** Always separate recurring EBITDA from one-off cash, and say that the saving applies to addressable spend.

INT.VO.2.a · Planning, monitoring, management and governance

Set out a value creation plan and a 100-day plan, build a KPI dashboard of leading and lagging indicators with cash conversion, and diagnose a portfolio company that misses plan.

The value creation plan turns the value bridge into a list of initiatives, each with a quantified EBITDA or cash effect, an owner, a timeline, a cost to achieve, and a risk. The 100-day plan is the first stretch of it: put cash visibility and reporting in place (a 13-week cash forecast and a monthly pack), confirm the team and owners, agree the baseline, launch quick wins, and set the governance rhythm. A KPI dashboard mixes lagging indicators, which report results already achieved such as revenue, EBITDA and cash, with leading indicators, which move first, such as pipeline and win rate, order book, price realisation, churn signals, on-time delivery and vacancies. Cash conversion is commonly EBITDA less capital spending and working capital outflow, divided by EBITDA, and its definition should be written down and used consistently. A monthly board pack shows actual against budget and prior year, an EBITDA bridge, cash and net debt, covenant headroom, a reforecast, an initiative tracker with status and risks. When a company misses plan, split the variance into volume, price and mix, input costs and overheads, check cash and covenants, then ask whether the plan or the execution was at fault. When initiatives compete for limited management time and cash, rank by EBITDA gain, cost, speed and risk. Interview point: facts first, people second.

WORKED EXAMPLE: DIAGNOSING A MISS AGAINST PLAN

A portfolio company had an EBITDA plan of 12.0 and delivered 10.2. The variance has four causes: volume shortfall, price and mix, input cost inflation and overheads. Volume cost 1.5, price and mix added 0.3, input costs cost 1.2 and overheads came in 0.6 below plan. Capital spending was 2.0 and working capital absorbed 1.8 (plan: 2.0 and 0.6). Diagnose the miss and compare cash conversion with plan.

Answer: The 1.8 miss is explained by volume (-1.5) and input costs (-1.2), partly offset by overheads (+0.6) and price (+0.3). Cash conversion fell from about 78.3% to about 62.7%.

> **Interview tip:** Start with a reconciled variance bridge, then leading indicators and cash, and only then talk about management.

INT.VO.2.b · Planning, monitoring, management and governance

Assess and incentivise management (sweet equity, ratchets, leaver terms, when to change a CEO or CFO) and explain board governance and the role of the operating partner.

Investors usually back management with a package that aligns pay with the exit. Managers buy ordinary shares, often called sweet equity, alongside the fund's institutional strip, which is mostly preference shares or loan notes with a fixed accruing return plus some ordinary shares. Because the preferred return is paid first, the ordinary shares are geared to value created, so managers gain a large share of the upside on a small investment and lose their stake if value is not created. A ratchet raises management's share of the ordinary equity if investors reach a higher return, for example a target money multiple. Leaver terms deal with managers who depart: a bad leaver, such as someone who resigns early or is dismissed for cause, usually sells at the lower of cost and fair value, while a good leaver, such as someone leaving through death, ill health or redundancy, usually receives fair value, with details set in the shareholders' agreement. Change a CEO or CFO when the evidence points to capability or trust, not on one bad quarter, and plan interim cover and the leaver terms first. Governance runs through the board: investor directors, a chair, reserved matters, committees and a monthly pack. An operating partner challenges and supports management with experience, while management remains accountable for running the business. Interview point: incentives reward value created, not hours worked.

WORKED EXAMPLE: WHAT SWEET EQUITY PAYS

A buyout is financed with equity of 100. The fund holds preference shares of 90 accruing 10% a year, compounded, and ordinary shares costing 10 in total. Management own 20% of the ordinary shares, at a cost of 2, and the fund owns the other 80%. After five years the equity is sold for 300. How much do managers receive, and what happens if it is sold for only 150?

Answer: At a 300 exit management receive about 31.0 on a cost of 2 (about 15.5 times). At 150 they receive about 1.0 and lose half their stake.

Interview tip: Explain that the preference return comes first, so the ordinary shares are geared, and say what happens in both the good and the bad case.

INT.VO.3.a · Diligence, buy-and-build, ESG and exit

Run commercial and operational due diligence, size buy-and-build synergies and costs to achieve, and distinguish a turnaround from a growth situation.

Commercial due diligence tests the market and the plan: market size and growth, the company's share and position, customer concentration, retention and pricing power, competitors, and sensitivities of the forecast, often using customer calls and data. Operational due diligence tests the cost base, capacity and utilisation, supply chain, systems, capital spending needs, reporting quality and management depth, and it turns findings into an initial 100-day plan. Both look for what can go wrong in the plan, not only confirm it. In a buy-and-build, a platform company acquires smaller businesses, often at lower multiples than the platform is expected to command. That multiple gap is only value if the combined group is valued at the higher multiple, so it is not a plan on its own. Cost synergies such as procurement, back office and footprint are more controllable than revenue synergies such as cross-selling, which depend on customers. Value from an acquisition is the post-synergy EBITDA at the group multiple less the price paid and the one-off costs to achieve the synergies, which are often a multiple of the annual saving. Integration risks include management distraction, customer losses, systems and culture. A turnaround puts liquidity, a 13-week cash forecast and stabilisation first, while a growth situation puts investment in sales, product and acquisitions first. Interview point: size the downside case, not only the base case.

WORKED EXAMPLE: VALUING A BOLT-ON AND ITS DOWNSIDE

A platform is valued at 10.0x EBITDA. It buys a bolt-on with EBITDA of 5.0 for 30 (6.0x). Run-rate cost synergies are 1.5 a year and the one-off cost to achieve is 2.4. Ignoring financing, fees and any change in the platform's multiple, what value is created? What if only half the synergies are delivered and costs overrun by 50%?

Answer: The base case creates 32.6 (20 arbitrage, 15 synergies, 2.4 cost). With half the synergies and a 50% cost overrun it creates 23.9.

Interview tip: Say that cost synergies are more reliable than revenue synergies, that the multiple gap needs a buyer at the group multiple, and give the downside number.

INT.VO.3.b · Diligence, buy-and-build, ESG and exit

Identify ESG levers that create or protect value, and prepare a business for exit with a credible equity story and evidenced earnings.

ESG levers create value when they show up in cash flow, risk or access. Energy and resource efficiency cuts annual cost, safer operations reduce incidents, downtime and insurance cost, strong governance and data protect against fraud and surprises, supply chain standards reduce disruption, and credible sustainability credentials can win tenders or lower financing margins in sustainability-linked loans. Quantify them like any other lever with cost, saving and payback, and avoid claims that cannot be evidenced. Buyers at exit run their own ESG due diligence, and gaps such as missing emissions data or a worsening safety record can lower the price or lead to indemnities. Exit readiness starts 12 to 18 months before a sale: clean accounts and a quality of earnings view, vendor due diligence where useful, a track record of forecasts that were met, a ready management team and a tidy data room. Buyers pay for earnings that are real, recurring and evidenced, so they will adjust for one-off gains and for under-investment such as cut maintenance. The equity story explains why the business has grown and improved, with evidence, and why it has a credible next stage that a new owner can fund and capture. Routes include a trade sale, a sale to another fund, a listing and a continuation vehicle. Interview point: do not lift EBITDA before exit in a way a buyer will reverse.

WORKED EXAMPLE: AN ENERGY PROJECT AND A BUYER'S ADJUSTMENTS

A company spends 4.0 a year on energy. A project costing 3.0 will cut energy use by 25%, and the saving is metered. The exit multiple is 8.0x. Separately, a buyer reviewing reported EBITDA of 50.0 removes 2.0 for maintenance cut in the final year and 1.5 for a one-off contract gain, and adds back 0.5 of one-off restructuring costs. What are the value of the project and the effect of the buyer's adjustments at 9.0x?

Answer: The project saves 1.0 a year with a 3.0-year payback and creates 5.0 of value net of cost at 8.0x. The buyer's adjustments cut enterprise value by 27.0 at 9.0x.

> **Interview tip:** Quantify ESG like any other lever, and say that buyers pay for evidenced earnings and will reverse cosmetic gains.

Summary of the Charta interview-preparation topic. Companies and figures in the examples are invented. Draft content, not yet expert reviewed.