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Remaking American Manufacturing

KATHRYN MULLIGAN
Editor-in-Chief,
Middle Market Growth
kmulligan@acg.org

The U.S. elections are right around the corner, and middle-market manufacturers will undoubtedly be watching the outcome closely. Their industry intersects with globalization, job creation and innovation, making manufacturing a key issue of recent presidential campaigns.

In this manufacturing-themed issue of *Middle Market Growth*, we explore some of the opportunities and challenges that U.S. manufacturers face today. In our cover story on p. 24, we look at how organizations are rethinking where they make and source parts. For years, U.S. companies have looked to Asia as a low-cost production hub, but that's starting to change, due in part to tariffs and supply chain vulnerabilities revealed by the COVID crisis.

Bringing manufacturing supply chains closer to home has the potential to benefit American manufacturers, as well as the domestic labor force. Yet filling manufacturing positions might not be easy. Reporting from the *Wall Street Journal* showed that roughly 700,000 fewer Americans worked in manufacturing jobs in August than prior to the pandemic. But before that, manufacturers struggled to attract young workers, leading some to take proactive steps to close the talent gap through educational partnerships, internal training programs and more (p. 14).

Although manufacturing has failed to capture the imagination of young adults, technology has created the need for skills not typically associated with a factory floor, like AI, robotics and cybersecurity. Those jobs—and their high earning potential—could spark interest in manufacturing as a career path.

Technological advancements are also altering the opportunity set for investors. This issue spotlights two emerging subsets in manufacturing where private equity has taken an interest. One is 3D printing, a technology that has advanced in recent years, positioning it to play a greater role in the production process (p. 21). Another is space-related manufacturing, including the ability to make parts in orbit (p. 10). In both cases, private equity firms are betting on technologies with transformative potential and providing funding to scale these businesses.

The outcome of the 2020 elections will inform trade policy, research and development incentives, and employment regulations, all of which will affect midsize manufacturers. How companies adapt to these macro changes, harness technology and build their workforce will ultimately determine the future of American manufacturing. //

Kathryn Mulligan

ACG Readies for Change

MARTIN OKNER
Chairman, ACG Global Board of Directors, and President and COO, dpHUE

Like many of you, I didn't expect 2020 to shake out the way it did. I began my term as chairman of the Association for Corporate Growth in September 2019, expecting to work with ACG's new CEO, Tom Bohn, to strengthen the organization as the home for middle-market M&A professionals.

We planned to unveil our growth strategies in person at InterGrowth, as part of a three-year plan. Instead, we went straight into execution mode—strengthening our digital platform, revitalizing membership engagement, growing our media assets, optimizing our governance, and advocating for the middle market. We accomplished what we thought would take two years in less than six months. Please join me in congratulating Tom and the ACG leadership team for their hard work and dedication to ACG members!

New initiatives this year included launching ACG's first-ever virtual dealmaking summit and introducing GrowthTV, ACG's video channel. We established an entire department dedicated to the membership experience. We updated ACG's governance structure to be more agile, and have decided to take the bold move to reduce our board to 15 members, down from 27. We also established our first-ever chapter council, to ensure local ACG leaders are represented in the organization's decision-making.

We know our members are asking similar questions about how to adapt to the modern economy. This issue spotlights manufacturing, an industry that is now scrutinizing supply chains and weighing the pros and cons of reshoring production. As someone who manufactures products myself, I can honestly say this edition of *MMG* is both timely and relevant as we look ahead to 2021 and beyond.

Grappling with changes of this magnitude requires access to resources and a network of peers and experts, and ACG continues to serve as that hub for the middle market. It's been an honor to serve as chairman over the past year and to help the organization adapt to the needs of its members.

ACG is now in a better place than ever to serve the middle market, but the work doesn't end here. Brent Baxter, managing director of Nolan & Associates, will take on the role of chairman in January. I believe under his leadership, working alongside Tom Bohn and the ACG leadership team, the organization is in good hands and that the best years are yet to come.

The world will undoubtedly keep changing, and ACG is ready to evolve along with it. Thank you for being members and for your dedication to the long-term success of ACG. //

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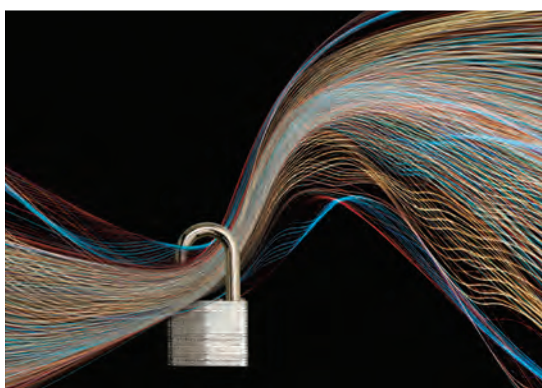
COVER STORY

All Ashore

Tariffs and supply chain disruption from COVID-19 are accelerating the trend toward "reshoring," as companies consider working with domestic suppliers over manufacturers in Asia. With help from their private equity owners, some middle-market companies are reconfiguring their supply chains to preserve working capital and shield themselves from risk, while others are ramping up to meet the growing demand for American-made products. 24



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TREND

Retooling Factory Security for the Digital Age

A cybersecurity breach can result in stolen trade secrets or costly factory shutdowns, yet many midsze manufacturers lack the proper security infrastructure and protocols to shield themselves—or a future owner—from the fallout of a hack. 32

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MMG CONVERSATIONS

Inside the Deal: HKW & Fresh Direct Produce

On the podcast, members of private equity firm HKW describe working with their portfolio company Fresh Direct Produce to acquire another Canadian produce distributor this summer, and how they overcame challenges related to the pandemic as they finalized the deal. Fresh Direct Produce's president and co-founder joins them to discuss the strategy behind the acquisition, and why demographic changes in Canada are a key driver behind his company's growth.

PODCAST Listen to this interview and previous episodes at middlemarketgrowth.org.

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EDITOR-IN-CHIEF
Kathryn Mulligan
kmulligan@acg.org

PRESIDENT & CEO
Tom Bohn, CAE, MBA
tbohn@acg.org

VICE PRESIDENT, ACG MEDIA
Jackie D'Antonio
jdantonio@acg.org

MANAGING EDITOR
Phil Albinus
palbinus@acg.org

DIRECTOR, CREATIVE & BRANDING
Brian Lubluban
blubluban@acg.org

MANAGER, CREATIVE & BRANDING
Michelle McAvoy
mmcavoy@acg.org

ASSOCIATE EDITOR
Benjamin Glick
bglick@acg.org

CHIEF OPERATING OFFICER
Matthew Hickman, MBA
mhickman@acg.org

VICE PRESIDENT, SALES
Harry Nikpour
hnikpour@acg.org

DIRECTOR, STRATEGIC DEVELOPMENT
Kaitlyn Fishman
kfishman@acg.org

Association for Corporate Growth
125 South Wacker Drive, Suite 3100
Chicago, IL 60606
membership@acg.org
www.acg.org

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When Owners Roll: Creating Alignment Between Management and PE

ELIE AZAR

Title: Founder, CEO and Managing Director

Company: White Wolf Capital LLC

Location: Miami, FL

Expertise: Elie Azar is a seasoned private equity professional, drawing on a career that spans over 20 years of M&A and private equity investing experience. Prior to founding White Wolf in late 2011, Azar worked at Cerberus Capital Management, Ernst & Young and Arthur Andersen.

▸ Does your firm have a playbook for aligning management interests with those of investors?

We are flexible as to how our portfolio companies achieve alignment with investors across management ranks; however, every approach shares the same DNA. First, we ensure that there is a clear strategic plan for value creation based on the investment thesis for the original investment.

In the case of founders (sellers) who wish to stay on and help drive growth post acquisition, we look for a substantial commitment via "rolled" equity—somewhere in the 20% to 35% range. We want these highly successful entrepreneurs—now our partners—to understand that their "second bite at the apple," combined with the proceeds from the original transaction, can generate significantly more personal wealth than what they had hoped to achieve from the original sale.

Upon closing, we work with our partners to refine the strategy and translate it into annual plans with specific operating and financial goals. Managers participate in shaping the annual plan and those with equity clearly have a stake in achieving those plans.

▸ How do you decide who receives preference when structuring the ownership positions among various kinds of equity holders, such as investors and key managers?

We don't! We invest in the same security as management (mostly common equity). The reason is rooted in one of our firm's bedrock values: partnership. We believe that the best engine for maximizing value creation is a committed core team bound by the principle that every member is a partner and every partner is treated equally regardless of the size of their slice of the pie. Every partner has a voice in shaping a common ownership vision and each is motivated to maximize value. All partners are pari passu—side by side—when it comes to distributing rewards. This is in sharp contrast to preferred equity where some owners are at the front of the line.

▸ How do you determine whether or not a member of the management team of a portfolio company receives equity in the deal?

That's an easy one—we always welcome any manager or key employee to participate alongside us as investors. Having "skin in the game" is arguably the most potent way to drive alignment, focus and motivation. We also set aside a pool of equity for key managers awarded either as inducements to join our teams or as recognition and reward for delivering value. //

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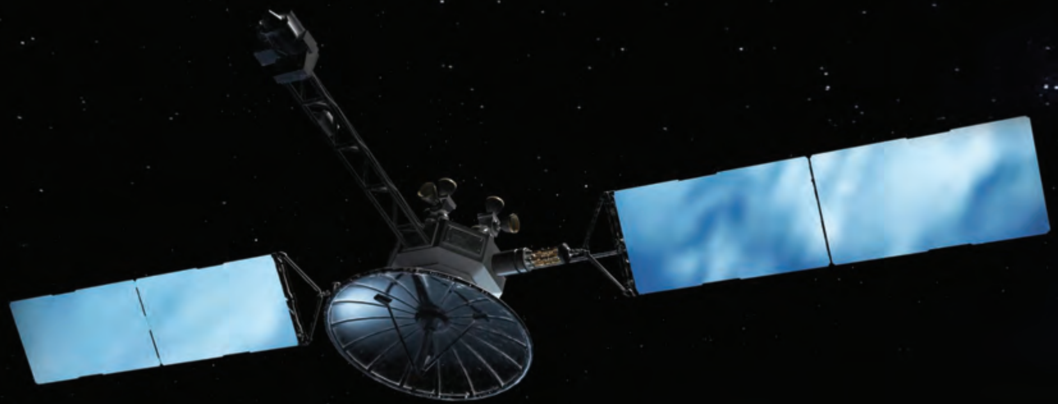


The Middle Market's Next Frontier

Smaller satellites and in-orbit manufacturing are sending more companies into space

By Benjamin Glick

At his home office in Boca Raton, Florida, Marc Bell picks up a polished black box from his desk.

"This is why the world changed," says the founder, president and CEO of investment firm Marc Bell Capital Partners, holding something a little bigger than a Rubik's cube. "This is what made space travel affordable."

Weighing around six pounds, the pint-sized satellite in Bell's hand was designed and built by Tyvak Nano-Satellite Systems, a subsidiary of Terran Orbital, of which Bell is co-founder and chairman. A version of the satellite platform, the Trestles 6U, launched into orbit in December 2019, and it's one of the innovations leading more companies into space by drastically reducing the weight—and therefore cost—of getting into orbit.

Not long ago, space was the exclusive domain of publicly funded initiatives and a few large private players, but declining costs from breakthroughs like Tyvak's miniature satellite, SpaceX's partially reusable Falcon 9 rocket and the development of in-orbit manufacturing are opening up space to more private companies and drawing interest from investors.

A 2018 estimate from the Space Frontier Foundation, an advocacy group that supports the private space industry, valued the total annual revenue generated by companies that produce spacecraft or collect and analyze satellite data at around $350 billion. Reports from Goldman Sachs, Deloitte and Morgan Stanley project the space industry could reach $1 trillion to $2 trillion by the 2040s.

Investors have spotted the opportunity. In 2019, there were 159 disclosed deals in the space technology sector, a nearly 10% increase from the year before, according to data from PitchBook. One of the largest deals was the $110 million venture round for the Sierra Nevada Corporation, a designer and maker of hardware like space suits and spacecraft components.

Despite a downturn in M&A due to the pandemic, this year's deals include the $1.64 billion acquisition of satellite imaging firm Dynetics by Leidos, an aerospace and defense company.

Filling the Middle Space

Like many cutting-edge industries, the space technology industry has a bookending problem. Peter Cannito, chairman and CEO of Redwire, a spacecraft component manufacturer, describes it as akin to a barbell: big companies on one end, early-stage ventures on the other, and not much in between.

"You either have large, legacy aerospace organizations that struggle to adapt rapidly enough to new innovation, or small companies that don't have the scale to take on major programs or move disruptive technologies into production," Cannito says.

The imbalance between startups and incumbents also poses a challenge for investors, he adds. "It means you have to invest in too many small transactions in order to move the needle, and there are no new entrants capable of producing above-average returns at scale."

Redwire's goal is to fill the middle-market gap in space technology with a company small enough to innovate rapidly, but large enough to finance major programs and production contracts.

Cannito joined Redwire shortly after it was created in March by AE Industrial Partners, a private equity firm that invests in midsize aerospace and manufacturing companies.

A former operating partner at AE, Cannito joined Redwire to manage its acquisitions, the first of which came in March with Adcole Aerospace, a nearly 60-year-old company that had produced components for most major NASA space missions, including the Perseverance and Ingenuity Mars missions that launched in July.

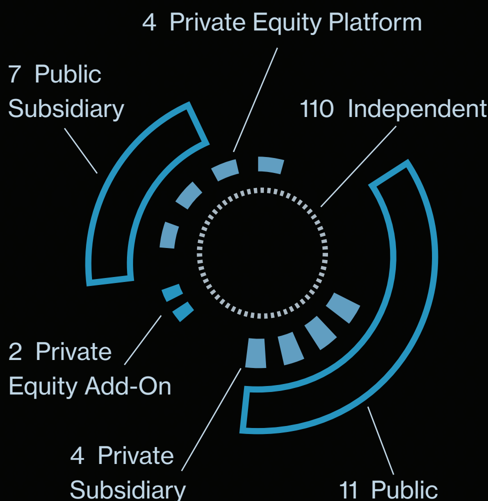
In June, Redwire acquired aerospace designer and manufacturer Deep Space. A few weeks later, it announced the acquisition of Made In Space, a company that got its start working on the International Space Station, developing techniques to manufacture components in orbit.

Cannito draws parallels between Redwire's motto, "Heritage Plus Innovation," and its goal of taking companies that excelled in one area and integrating them under a single platform.

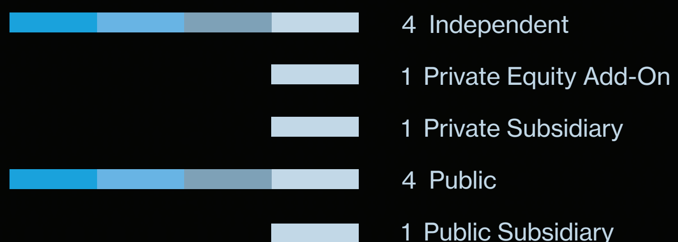
"We don't consider ourselves to be just a new space disrupter," he says. "Our thesis is to combine flight heritage with some of the disrupters to fill that middle-market gap."

The combination of legacy companies like Adcole and new players like Made In Space enables Redwire to carry out large-scale programs, like the 2020 Mars mission, while also fostering innovations like in-orbit manufacturing and miniature components for spacecraft. »

SPACE MANUFACTURING COMPANIES



IN-SPACE MANUFACTURING COMPANIES



FOOD IN SPACE

Information refers to the global space industry, provided by Grata Data

Private Equity's Opportunity

Only a handful of private equity firms have a presence in the industry, and they tend to be big players like Blackstone, which bought a space-based optics business from defense giant Raytheon in April. But the continued commercialization of space and a market that has yielded many stable, late-stage startups is changing that.

"It's become an opportune time for private equity to be able to invest," says Kirk Konert, a partner at AE. "The market has matured enough for the industry-focused firm to find interesting opportunities, companies and teams to back."

At press time, there are more than 100 independently owned companies that manufacture components for the space industry, including 90 based in the U.S., that could make attractive targets for investors, according to Grata Data, a company search engine.

Konert adds that AE is bullish on recent developments shaping the space industry, like SpaceX's launch of the first manned mission completed by a commercial organization in May, and the creation of the U.S. Space Force, which was established in December 2019 to protect the growing number of assets in orbit. "We're going to certainly be active," Konert says.

Launching the Space Economy

Konert and Cannito expect Redwire will continue working with government agencies like NASA and the Department of Defense to generate consistent cash flow. Over the long term, they want to expand the company's customer base to include other commercial entities.

"WE DON'T CONSIDER OURSELVES TO BE JUST A NEW SPACE DISRUPTER. OUR THESIS IS TO COMBINE FLIGHT HERITAGE WITH SOME OF THE DISRUPTERS TO FILL THAT MIDDLE-MARKET GAP."

PETER CANNITO
Chairman and CEO, Redwire

Redwire has taken note of several high-profile setbacks in the industry, including bankruptcy filings by satellite communication providers OneWeb and Iridium Communications, whose business models proved costlier and less lucrative than expected, according to Cannito.

"Physics will get you to space, but economics will keep you there," he says.

To ensure it remains financially sustainable, Redwire is looking to provide companies with infrastructure—new space-based communications and capabilities to manufacture components in orbit—something it hopes to achieve with its Made In Space acquisition.

In-orbit manufacturing could significantly reduce the cost to launch satellites and expand their capability. A satellite that can print its own solar panels or antennae in orbit could generate more power and have greater communications capacity in a smaller package, Cannito says, and could be the key to unlocking larger projects like commercial research and development outposts, and resource extraction on the moon.

Although private equity is still relatively new to the space industry, firms like AE Industrial are entering on the heels of early investors, like Marc Bell, who helped pave the way. In 2015, Bell was among the first to commit seed funding that got Made In Space off the ground.

Bell has been involved in the space technology industry since the 1990s, and his companies have since put over 220 satellites in orbit. His current venture, Terran Orbital, a provider of nanosatellite and microsatellite services, was founded in 2013 and is now valued at $60 million and has 125 employees. Its subsidiary PredaSAR announced in August that it will partner with SpaceX to deploy the first of 48 planned satellites next spring to collect data about activity on Earth's surface—from weather and agriculture to traffic and energy extraction.

Over his 30-year involvement in the industry, Bell has seen how the miniaturization of satellites changed the economics of space. The influx of capital from investors like AE Industrial is now funding further innovation, like in-orbit manufacturing, an advancement that Bell expects will help shape the future of the space industry.

"It's definitely going to start changing things," he says. "We'll know when you can lay out on the beach on Mars." //

How Manufacturing Has Adapted to the Pandemic

ACG Chicago panelists discuss coping with the crisis and its long-term impact

By Benjamin Glick

The COVID-19 pandemic upended manufacturing, causing declining demand, rising costs and disrupted supply chains. During a virtual panel session hosted by ACG Chicago in September, manufacturing experts looked back at how manufacturers have adapted to those shocks and discussed their long-term impact.

Joe Zito, a partner at management firm The Keystone Group, said some of his manufacturing clients are still struggling with anemic demand, but few are resorting to laying off employees.

The post-outbreak demand crunch may have alleviated some pressure for skilled labor, but Zito said companies want to avoid future shortages once an economic recovery takes hold. They would rather cut hours and pay than lose workers.

Keystone's clients are also investing in new technologies, like tools to collect productivity data.

Zito cited one finding from early data analysis that suggests cutting back on labor does not correspond to a proportional decline in factory output. When one client cut back on labor by 20%, it saw only a 10% reduction in output.

Harry Moser, founder of the Reshoring Initiative, a Chicago-based nonprofit, discussed the trend toward sourcing workers and suppliers locally, rather than abroad—known as reshoring—and its impact on manufacturing.

The total number of jobs created by reshoring and foreign investment in the U.S. climbed to 190,000 in 2017 from 6,000 in 2010, according to the Reshoring Initiative's research.

> “WE WERE FULLY CHALLENGED IN ALL AREAS—AIR, OCEAN, GROUND AND EVEN RAIL.”
>
> VAUGHN MOORE
> President and CEO, AIT Worldwide Logistics

It attributes that increase to tax and regulatory reductions in the U.S. and rising wages in China.

One of the tools the nonprofit provides to manufacturers looking to bring operations closer to home is its total cost of ownership, or TCO, estimator, which factors in many of the hidden costs companies operating overseas often miss—travel costs, import duties and risk to intellectual property.

Using the metrics companies typically employ when estimating the cost of doing business abroad, only about 8% of U.S. companies were cost-competitive in market research. Using the TCO estimator, the Reshoring Initiative was able to increase it to 32%.

“Our biggest challenge is to convince companies to do the math correctly,” Moser said.

Donna Dorsey, the chief human resources officer of Navistar, a multibillion-dollar automotive manufacturer based in the Chicago area, said her company faced a breakdown in its global supply chain as suppliers closed their doors or cut back production.

In the U.S., the first peak of coronavirus cases occurred in early April, but in Brazil and Mexico, where Navistar's overseas operations were hit hardest, the peak didn't occur until late July, making it difficult to coordinate transportation logistics.

Navistar responded by putting together a team that tracked critical suppliers. The team corresponded with company leaders in each country and gave them reins to respond independently.

“At the end of the day, our in-country leaders are closer to what's going on,” Dorsey said.

Discussing the impact the coronavirus has had on the logistics industry, Vaughn Moore, president and CEO of AIT Worldwide Logistics, said difficulties have spanned all modes of shipping and transportation.

“We were fully challenged in all areas—air, ocean, ground and even rail,” he said.

After capacity collapsed at the start of the pandemic, most freight carriers had to dramatically raise rates to make up for losses.

Ahead of the holiday season, when many manufacturers see peak demand, those rising rates could eat into profits, Moore said. That, in turn, could be bad news for small logistics companies, many of which could close as demand for transportation declines.

However, Moore says it could be an opportunity for M&A, as he foresees a lot of consolidation in the logistics industry. “Goods always have to get from point A to point B,” he said. //

Closing the Talent Gap

How two companies are helping to combat manufacturing's worker shortage

By Benjamin Glick

Matthew Davis has a passion for developing talent. It's what he built his career on, and he's now applying that enthusiasm to help address the skills gap in manufacturing at a critical time.

Raised in Argos, Indiana, a city of just over 1,600 residents, Davis recalls visiting his father, uncle and grandmother while they worked at ITAMCO, a maker of gears and other components used in the mining, energy and defense industries.

GETTY IMAGES/SAROTE PRUKSACHAT

Today, Davis is putting his passion for developing others to use as the training and organizational development manager and head of community outreach for ITAMCO.

Like many other communities across the U.S., Plymouth has struggled to attract and retain manufacturing talent.

"I've got three kids. What does the future look like for them?" Davis asks. "How do we continue to lead the younger generation to fill the gaps that we're going to have here very soon?"

According to a report released in August by the Manufacturing Institute, an advocacy group focused on developing skilled workers, there were more than 500,000 unfilled manufacturing jobs in 2019 nationwide, a gap expected to grow to 2.4 million by 2028.

The Manufacturing Institute estimates that the value of the U.S. manufacturing sector is projected to increase by $454 billion by 2028. If nothing is done to close the talent gap, it could be at risk. Manufacturers appear to be responding with a range of strategies, including internal training programs—an approach that 78.8% of respondents to a 2019 Manufacturing Institute survey said they're using to ensure they have the right skills on staff.

Midsize manufacturers cited talent management as the second-biggest source of risk to their company, behind only competition, according to a 2018 report from insurance provider Chubb, produced in partnership with the National Center for the Middle Market. Respondents listed finding workers with the technical skills needed for job openings as the single biggest challenge facing their workforce.

That's a problem, but not one that falls on all companies equally, Davis says. ITAMCO's larger competitors may be able to increase wages and pull skilled workers away from middle-market manufacturers with smaller budgets.

Since joining ITAMCO in 2018, Davis has helped lead the company's talent development efforts, which have included partnering with area high schools, donating machinery and equipment, and developing educational programs for students.

Manufacturers have struggled to convince younger people to fill entry-level positions, like machine operators. Leading2Lean, a manufacturing software company, found in a 2019 survey that 68% of millennials (those born between 1981 and 1998) agreed that manufacturing jobs are important to the economy, compared with 86% of respondents from older generations.

Davis has helped organize educational events in Plymouth and beyond in the hopes of yielding more talent for ITAMCO, including seminars and workshops organized in partnership with the University of Notre Dame and regional economic development organizations.

Although hiring for some positions has declined during the pandemic, Davis says new clients have reached out to ITAMCO to supply

components, part of a broader trend of bringing supply chains back to North America.

"We're viewing the virus almost as a blip. We think more work is coming right behind it," Davis says.

That's putting more pressure on ITAMCO to find skilled workers, like machinists, database engineers, app developers and supervisors. Without them, the company will reach capacity and have to turn down new work.

To make the costs of doing business in North America comparable to low-cost markets like China, manufacturers will likely need to leverage technologies like automation, data analytics and artificial intelligence.

As machines take over repetitive tasks once assigned to humans, workers will need to be trained to use digital tools in addition to "soft skills" like critical thinking, creativity and people management, according to a report from Deloitte.

An Innovative Culture

The challenge of recruiting has led some manufacturers to hire candidates without direct experience in the field, and to help them obtain the specific skills needed for their jobs.

Design Ready Controls, a manufacturer of control panels for large machines headquartered in Brooklyn Park, Minnesota, is among the firms to embrace this approach.

"When you're looking to build your organization, you've got to start with your staff first," says Andy Smith, DRC's talent management specialist.

The vast majority of DRC's 400-plus employees don't have backgrounds in manufacturing, he adds. The company doesn't focus on expertise; instead, it selects candidates who will be self-motivated.

"YOU NEED TO HAVE AN EMPLOYEE BASE THAT IS LOOKING TO FURTHER DEVELOP THEMSELVES AND CREATE THEIR CAREER PATH WITHIN THE COMPANY."

ANDY SMITH
Talent Management Specialist, Design Ready Controls

"You need to have an employee base that is looking to further develop themselves and create their career path within the company," Smith says.

In some cases, DRC provides financial support, like tuition reimbursement, to help employees grow; in others, it offers training to ease the transition into a new role, as well as opportunities to advance—a process known as upskilling.

About three-quarters of respondents to the Manufacturing Institute's 2019 survey said upskilling workers helped to improve employee productivity. Manufacturers are set to spend $26.2 billion on upskilling and other training initiatives for new and existing employees in 2020 to combat worker shortages, according to the organization.

DRC's talent management strategy has evolved over the years, but it can trace its start to 2015, when the company began receiving support through Minnesota's Dual-Training Pipeline grant program, designed to foster job creation in the state.

DRC has also joined Summit Academy OIC, a Minneapolis-area nonprofit that provides skilled job training for students. The Summit-Design Ready Controls initiative is an entry-level program designed to provide training in the electrical fabrication field, with instruction conducted via a combination of classroom and on-the-job training. The 20-week program concludes with a two-week internship at Design Ready Controls, which doubles in part as a job interview. Sixteen students per year are anticipated to be hired at Design Ready Controls as point to point wirers, power wirers or control box builders.

The number of electrical and electronics engineering jobs—which include electrical technicians—is projected to grow 3% from 2019 to 2029, according to the Bureau of Labor Statistics, leading to more than 10,000 openings nationwide over the next decade.

Despite the disruption caused by the coronavirus, DRC was able to continue its talent development programs by moving interviews, training, tours and even job fairs online or over the phone. Ultimately, it hired 40 employees, who trained onsite in frequently cleaned rooms with limited personnel.

During the nationally recognized Manufacturing Month in October, DRC's facilities in Minnesota and Virginia are partnering with area schools to raise awareness of manufacturing careers. Previously, the events were only accessible to students in their local areas. Now that they've moved online, students across the U.S. can join, too.

"The right talent is out there, but we've just got to find creative ways to find them," Smith says. //

ACG Western Michigan Recognizes Bradford Company for Outstanding Growth

By Kathryn Mulligan

This year has prompted many businesses to begin exploring ways to retool their operations to stay relevant.

For Bradford Company, a manufacturer based in Holland, Michigan, innovation was a priority long before COVID-19, and it's contributed to the sustained growth that led ACG Western Michigan to honor Bradford as its 2020 Outstanding Corporate Growth Award winner during a virtual ceremony in August.

The fifth-generation family-run company makes packaging used primarily in the automotive industry. Customers use Bradford's industrial chipboard partitions and custom engineered reusable and returnable interior protective packaging solutions to transport auto parts between original equipment manufacturers and their suppliers.

Bradford's packaging is used to ship headlamps, door panels and "really anything with a Class A-friendly service that needs to be protected," said Tommy Bradford, a member of the Bradford family and the company's director of operational support, speaking during a video about the company broadcast during the award ceremony.

The company prides itself on working with customers to develop packaging solutions that meet their needs.

"I think what's separated us in the industry is the horsepower that we have, and the responsiveness we have to our customers," said Tom Bradford, the company's president and CEO, and a fourth-generation member of the Bradford family, during the video.

Originally founded in 1897 as W.J. Bradford Paper Company and incorporated in 1924, the company today operates eight manufacturing locations across North America.

That expansion reflects the owners' vision for the company. "Some families run their business as a lifestyle. We were ingrained to run the business as a business," Tom Bradford said. "We have the ability to think generationally, in terms of years rather than three-month quarterly reports."

The company has embraced a culture of innovation, with an eye toward working with customers to solve problems, while also finding ways to improve Bradford's internal operations.

"Our entire organization operates in a job-shop environment. We're able to dance on our feet to be able to come up with not only a product

"I THINK WHAT'S SEPARATED US IN THE INDUSTRY IS THE HORSEPOWER THAT WE HAVE, AND THE RESPONSIVENESS WE HAVE TO OUR CUSTOMERS."

TOM BRADFORD
President and CEO, Bradford Company

solution, but also a solution internally to allow us to reduce our overhead," said Tim Bublitz, vice president of engineering. "We're very proud to be that leading edge of our industry."

Bradford's performance caught the attention of ACG Western Michigan, which awards a local company each year that demonstrates sustained growth in sales, profitability, employment and community involvement.

In past years, ACG Western Michigan has hosted an in-person awards event in March to honor the Outstanding Growth Award winner and finalists. But the pandemic forced it to postpone the ceremony to August, and ultimately to change the format to a virtual event.

Still, ACG Western Michigan found a way to present the Bradford team with an engraved crystal award, which identified Bradford and the prior 16 winners by year in which the award was won. ACG shared that presentation via a pre-recorded video played during the awards event.

Although not the awards presentation ACG Western Michigan envisioned at the start of the year, the virtual adaptation was a fitting tribute to a company that's built its success on creative problem solving and a willingness to learn and evolve in an ever-changing market.

"We spend a great deal of energy to stay in front of it," said Bublitz. "We learn from the failures, then go again." //

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CASE IN POINT

WIPFLI LLP

Proven Partners

Guiding a PE-backed food contract manufacturer through its first audit and beyond

Consumer packaged goods brands had to adapt quickly in the early days of the pandemic in response to disrupted supply chains and surging demand, but their efforts to become more agile predated COVID-19.

Food and beverage brands in recent years have sought to introduce new products more quickly, redesign packaging, and expand sales channels—trends that Tilia Holdings, a private equity firm based in Chicago, was well-aware of when it acquired Proven Partners Group, a contract manufacturing and packaging business that works with leading CPG brands.

As the lower middle-market company's first private equity partner, Tilia knew that favorable market trends alone wouldn't guarantee success, and that growing PPG would require operational support, additional resources and the right advisory partners.

Founded 16 years ago in Elgin, Illinois, PPG specializes in the production of dried and powdered foods like coffee, protein powders, baking mixes and meal-replacement powders. It blends those ingredients on behalf of its CPG customers, then packs them into single-serving containers, canisters or other finished packages that are then shipped to retailers.

PPG's industry is poised for rapid growth, outpacing even the food and beverage sector. The contract food manufacturing industry has been growing at more than double the rate of the CPG sector, according to J.D. Elder, a vice president at Tilia. The Contract Packaging Association, an industry trade group, estimated the contract manufacturing and packaging industry serving the U.S. CPG sector was worth $25.67 billion as of 2018.

PPG's founders were looking to transition out of their day-to-day roles when they sold the business to Tilia in February 2019. PPG fit squarely within the private equity firm's focus on business-to-business service companies operating within the food supply chain, and Tilia saw an opportunity to expand production capacity and strengthen the company's commercial efforts.

After closing on the transaction, Tilia quickly hired PPG's first chief financial officer, Ron Markle, to ensure the company had the leadership infrastructure needed to achieve its growth objectives. With new private equity owners and a CFO on board, the company embarked on its next major undertaking: its first-ever financial audit.

NO BAIT AND SWITCH

Although PPG's financials had been reviewed in the past, the company had never gone through a formal audit process.

As it sought the right audit

partner, Tilia was introduced to Wipfli LLP, a national top 20 assurance, accounting, tax and advisory firm that PPG's prior owners had worked with on the company's tax returns. Wipfli knew PPG's business well, and its understanding of private equity and the manufacturing industry positioned it as a strong advisory partner.

Tilia ultimately selected Wipfli for the project, and work began in the fall of 2019. "By the time the transaction closed and they selected an audit firm, we had less than six months to get through the purchase accounting, adoption of revenue recognition and year-end audit," says Kevin Owens, a partner in Wipfli's Private Equity Services group, who led the team working with PPG.

Despite the tight timeline, Wipfli was able to complete the audit in February. "They were proactive in getting a head start on it and getting it done," Elder says. "We were very impressed with their work. It was timely, cost-competitive, and they really helped PPG through the process of doing that first-time audit."

Unlike some of its larger competitors, Wipfli offers a personal touch. Owens' message to clients is, "I am going to be your audit partner on the job. This isn't a bait and switch to bring out our technical expertise or people who know your industry, and know private equity, then give you another partner in the firm," he says.

Tilia experienced that commitment firsthand.

"Kevin, who oversaw the project, continued to be involved throughout," Elder says. "The team we thought would be working on the project really did lead the engagement."

A FLEXIBLE APPROACH

PPG is one of the fortunate businesses that has continued to grow in 2020. Since Tilia bought PPG, the company has nearly doubled its production capacity and is seeking to expand its capabilities and geographic presence through M&A.

Meanwhile, it continues to add new customers. For large CPG brands, PPG can help manage low-volume production runs that the customer's own equipment isn't designed for. PPG also presents an alternative for companies that don't want to invest in the infrastructure necessary to get their products to market.

Part of PPG's appeal for Tilia was its strong customer relationships and reputation for quality and safety—both of which have proved essential to navigating disruption from COVID-19. Wipfli has also played a key role in helping the company through the challenges of this year. Its team has responded to questions from PPG's CFO about structuring contracts, for example, and the implications for the company's EBITDA or income statement.

"The C-level has grown to trust our advice and what's going to happen in the future of their business," Owens says.

The challenges related to the pandemic have underscored the value that trusted advisers bring to their clients.

"With Wipfli, although we engaged them specifically do to the audit and tax returns, they've also been timely in responding to questions we have," Elder says. "It's been important for firms to build a broader partnership and relationship, beyond the specifics of an engagement, during COVID, and I think that will continue to be the case. //

"THE C-LEVEL HAS GROWN TO TRUST OUR ADVICE AND WHAT'S GOING TO HAPPEN IN THE FUTURE OF THEIR BUSINESS."

KEVIN OWENS
Partner, Wipfli LLP

J.D. ELDER
Vice President, Tilia Holdings

ACG Toronto's "Leadership Discussions Series" Panel

"In my opinion, in private equity your highest value-add, and sometimes your only value-add, is making sure you have the right people running the organization. The strategy is critical, but strategy doesn't really get anything done; it's the team that gets things done."

NED TRUSLOW,
Managing Director, RFE Investment Partners, on the importance of hiring strong portfolio company leaders

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You can't just have change for change's sake. There has to be a reason that everybody understands why things are changing. On the other hand, businesses are always changing ... I think [change management] should be incorporated as part of your business. As long as you understand where you're going, you should be able to accept those changes."

JEFF ROME,
Former CEO of Impact Confections, on how companies can effectively manage change within their organizations

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"Sometimes you do things to keep engaging people – they might be small wins but they help to fuel that continuous improvement engine – but good leaders cut through the nice-to-haves and the have-to-haves and focus on the things that are really going to drive the business forward."

ANDREW RUSH,
The panel's moderator and Vice President of Carpedia International Corp., which sponsored the Leadership Discussions series, on the lesson behind the adage, "Great leaders say no to things"

"TOLERATING MEDIOCRITY IN LEADERS SENDS A BAD MESSAGE AND ISN'T CONDUCIVE TO CREATING A HIGH-PERFORMING ORGANIZATION. I'VE ALWAYS FOUND IN MY CAREER THAT WHEN YOU FINALLY MAKE A CHANGE, THE PEOPLE BELOW GET ENERGIZED AND ASK, 'WHAT TOOK YOU SO LONG?'"

JAMIE BETTER,
Operating Partner, Kohlberg & Company, and CEO and Chairman of the board of directors of Nellson Nutraceuticals, on why retaining underperforming leaders is an obstacle to building a strong team

CORE Helps Industrial 3D Printing Take Shape

By Benjamin Glick

Additive manufacturing, also known as 3D printing, may be in its infancy, but that isn't stopping one private equity firm from investing now in hopes of producing components faster and at larger scales.

Unlike traditional manufacturing techniques that cut away raw material to create a new object, 3D printers deposit layer upon layer of metal, plastic and other materials to build a part from scratch.

Much of additive manufacturing is confined to startups that make one product, or large manufacturers that use the technology to augment production and prototyping. CORE Industrial Partners, a Chicago-based private equity firm focused on industrial technology, is taking a different approach.

In 2018, CORE acquired Midwest Composite Technologies, which acquired FATHOM, an additive manufacturing company based in Oakland, California. Along with a third 3D printing-focused manufacturer it purchased in August, CORE has brought together three facilities and nearly 100 3D industrial printers under the FATHOM brand. Combined, these companies make FATHOM one of the largest independent additive manufacturing companies in North America, according to CORE's Managing Partner John May.

Those assets enable the company to offer a wider range of services on a larger scale to its clients, including aerospace and defense, automotive and medical device manufacturers.

"We're building out this portfolio where you can go from prototype all the way to production," May says. "Through the combination of these companies that we've acquired and put under the FATHOM umbrella, we've got the expertise and technology to be able to solve virtually any customer's needs."

▲ One of FATHOM's manufacturing facilities with industrial-grade 3D printers

According to May, FATHOM's scale allows the company to reduce the time needed for design and production work from months to days.

Still, additive manufacturing has limitations. Technological gaps mean some components require traditional manufacturing methods like machining and injection molding. Industrial manufacturing can't yet accommodate all part sizes or large production runs.

There are also material constraints: 3D printing is currently limited to plastics and metals that melt at low temperatures. But technological advancements will likely enable the use of more materials and lead to better machines and higher levels of productivity, says May, who expects 3D printing companies to become more valuable in the future.

"We are seeing exponential growth of use cases where additive manufacturing allows our customers to combine parts, reduce weight and decrease the time to market," he says.

Additionally, FATHOM passed a critical test earlier this year amid the COVID-19 outbreak. As other manufacturers slowed or shuttered production during the pandemic, FATHOM was able to quickly retool its 3D printers to produce components for virus test kits, respirators and other critical medical supplies faster than traditional manufacturers.

"We leveraged our deep expertise to find acceleration points to meet the incredible demand," May says. "This is the beauty of the 3D printing business: You're able to very quickly respond to marketplace needs." //

"PERHAPS THE MOST IMPORTANT TAKEAWAY FOR MIDDLE-MARKET BUSINESS OWNERS IS THAT THE TRUE, INTRINSIC VALUE OF THE BUSINESS IS MORE THAN JUST A MULTIPLE OF REVENUE OR EBITDA."

Ari Fuchs

Managing Director, The DAK Group

Ari Fuchs is a managing director at The DAK Group, a middle-market investment bank headquartered in New Jersey. Fuchs specializes in the analysis and execution of M&A transactions, restructuring and strategic corporate advisory services. He has already closed two transactions during the COVID-19 crisis, with a number of others in various stages, yet targeted to close by year end or early 2021. He recently corresponded with *MMG* about the dealmaking climate for manufacturing businesses, and strategies for closing a deal during the pandemic.

Q How has the pandemic impacted buying opportunities in the middle-market manufacturing industry?

A The manufacturing industry was not immune to the disruption caused by COVID-19, and the subsequent slowdown of M&A activity in the first half of the year reflects that reality. While there were many bright spots in the manufacturing sector—including infrastructure, plastics and packaging, and food-related businesses—the pandemic-induced overhang substantially reduced the appetite for M&A. That said, we expect a pick-up in M&A activity in the second half of the year. Propelled by significant levels of private equity capital and corporate appetite for both transformative and tuck-in acquisitions, the middle market will be a direct beneficiary of the renewed levels of activity. Our own pipeline of manufacturing-related sell-side opportunities is robust and we are seeing a welcome level of eagerness and enthusiasm among strategic buyers and financial sponsors alike.

On the client side of the equation, we are definitely seeing more inquiries from tightly held family businesses, and in several instances multigenerational family businesses. Prospective sellers that were on the fence pre-pandemic have returned with a newfound willingness and desire to explore and engage in a sale transaction. Many business owners are being driven by the ongoing macroeconomic uncertainty and the desire to de-risk their overall financial picture by taking some chips off the table—a seemingly near-universal theme among our client base.

Q The coronavirus outbreak and trade tensions have illuminated supply chain weaknesses for many businesses. Has supply chain due diligence changed as a result?

A Manufacturing businesses have long recognized the economic and strategic benefits of third-party supplier relationships. These relationships are frequently the foundation of most of their day-to-day operations, providing them with a critical edge over the competition. Third-party suppliers provide an effective means for sourcing necessary expertise and resources without making costly investments needed to bring those capabilities or services in-house. Working with external suppliers, however, presents a series of challenges that must be thoroughly vetted. Pandemic-induced supply chain disruptions combined with the impact of trade tariffs has generated a renewed focus on product sourcing and supply chain efficiency, creating

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a new paradigm for supply chain due diligence in the context of M&A.

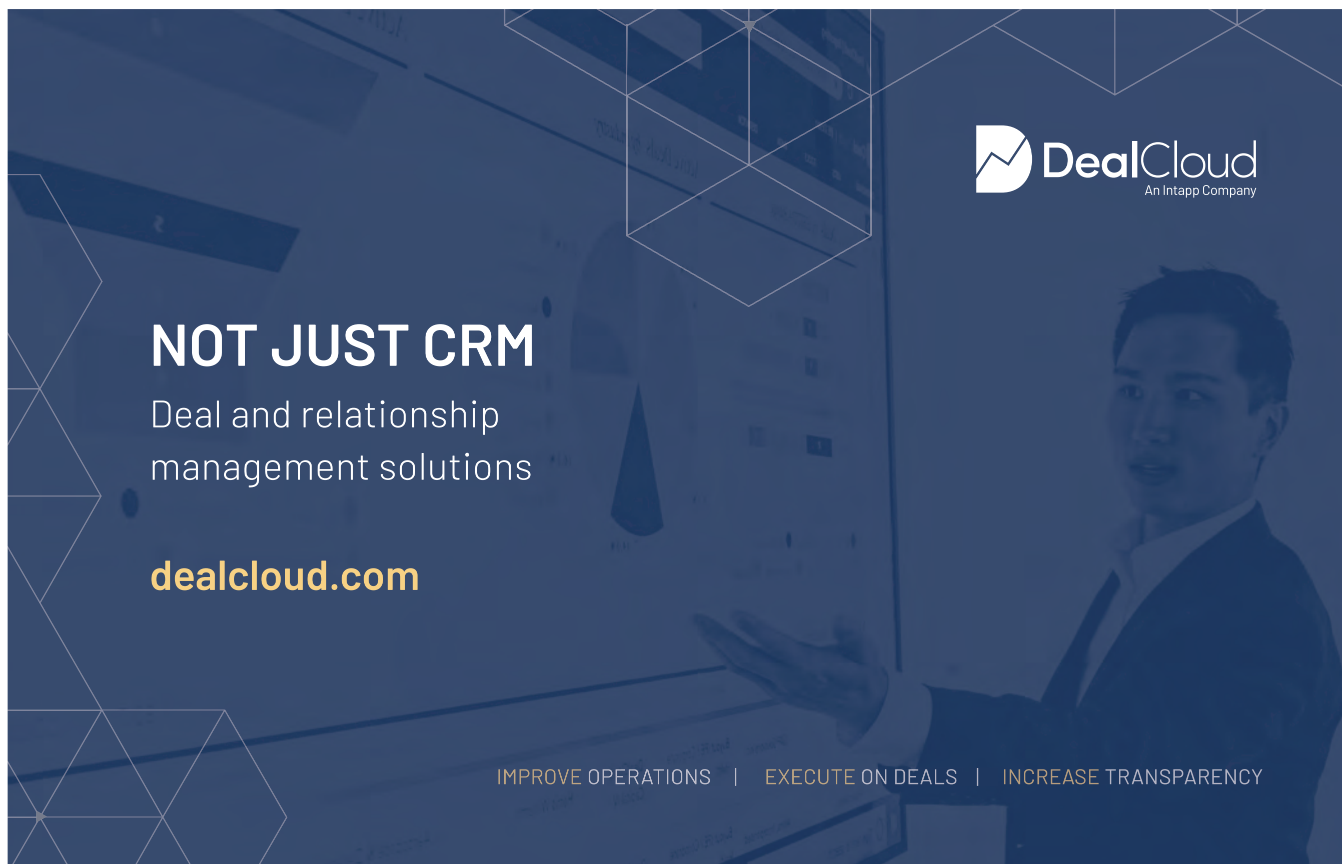
Supply chain due diligence has adapted to address these critical challenges. The diligence process has centered on certain key areas, such as evaluating country-specific supply chain risk, assessing the impact of force majeure clauses, evaluating supply chain flexibility in the face of possible further waves of the pandemic, as well as the availability and cost of alternative sources of supply.

Q How are you valuing companies in today's market, at a time when performance and future earnings estimates are clouded by COVID-19 disruption?

A It goes without saying that traditional valuation methods will have difficulty in accurately capturing business value in today's M&A environment. Unexpected increases or decreases in customer demand, fluctuation in the cost of raw materials, and unusual pandemic-related expenses are some of the factors that manufacturers are currently contending with. The long-term impact of the pandemic on corporate earnings and growth remains unclear. Making matters even more challenging is the sluggish financing market for M&A transactions. With lenders focused on protecting their existing loan portfolios, there is little appetite for new investments.

For today's middle-market business owner, this means the prospect of having to deal with depressed valuations, at least in the short term. It means deal structures are likely to change, with more earn-outs to share risk and larger equity backstops in leveraged deals.

But perhaps the most important takeaway for middle-market business owners is that the true, intrinsic value of the business is more than just a multiple of revenue or EBITDA. The true intrinsic value of a business is the value that it will bring to a strategic buyer and how it will enhance the overall earnings of the combined entity. The true intrinsic value of your business is not what it's worth to you, but rather what it's worth to a buyer. It's important to identify unique, out-of-the-box buyers, buyers in adjacent verticals, or cross-border buyers that can drive significant value from your business. Consequently, these types of buyers are likely to be in a position to pay more—perhaps even an outlier value. //



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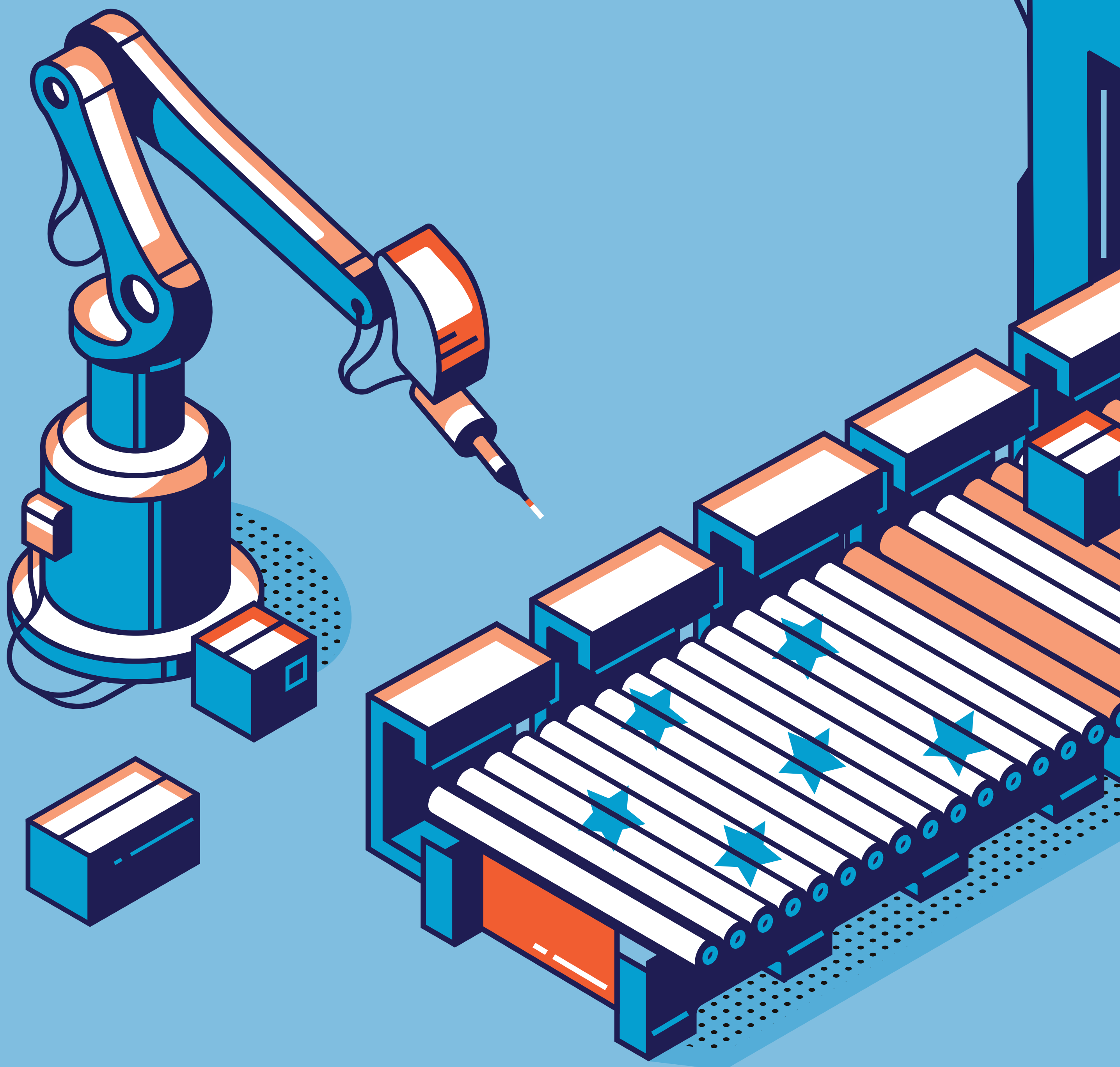
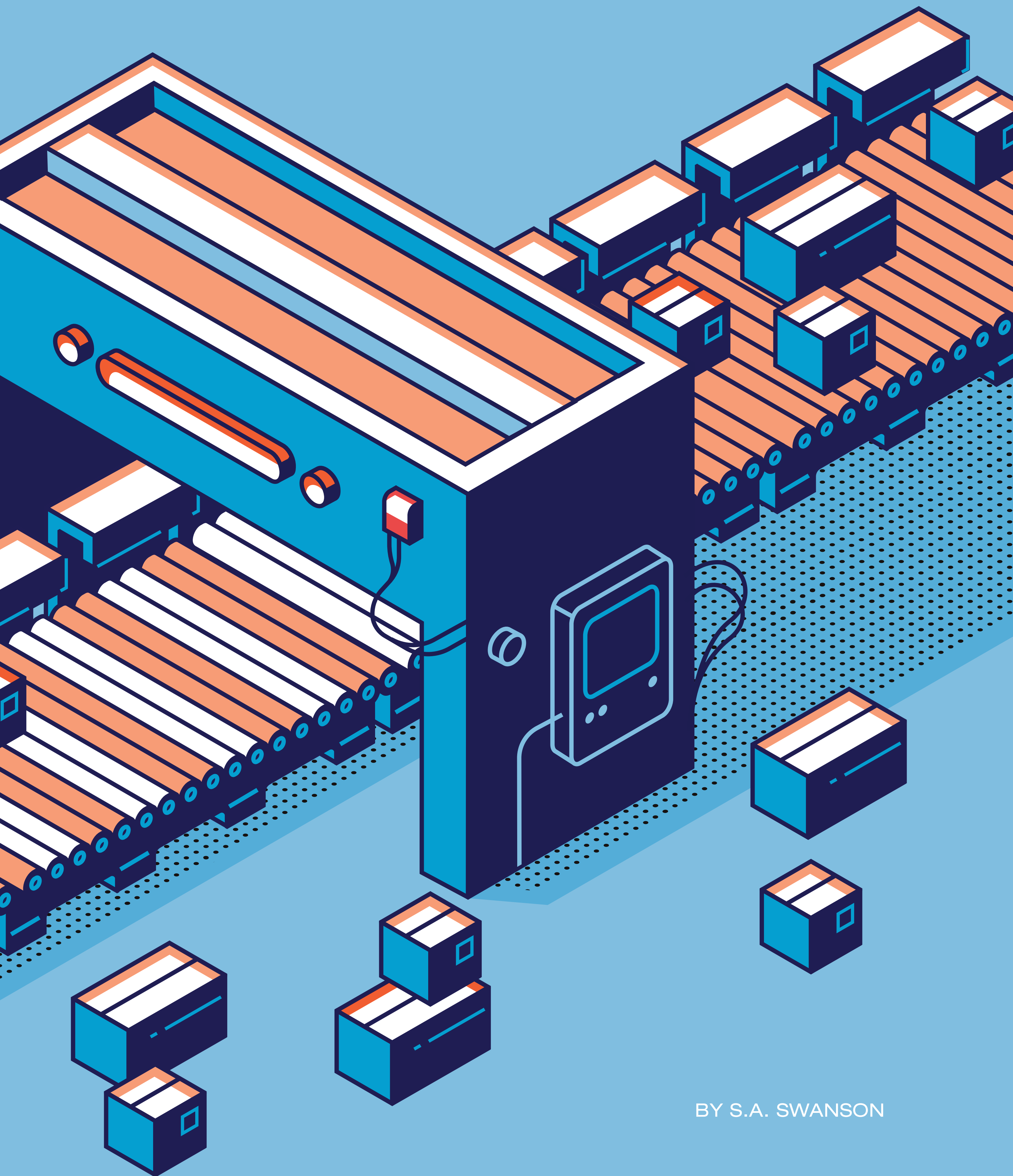
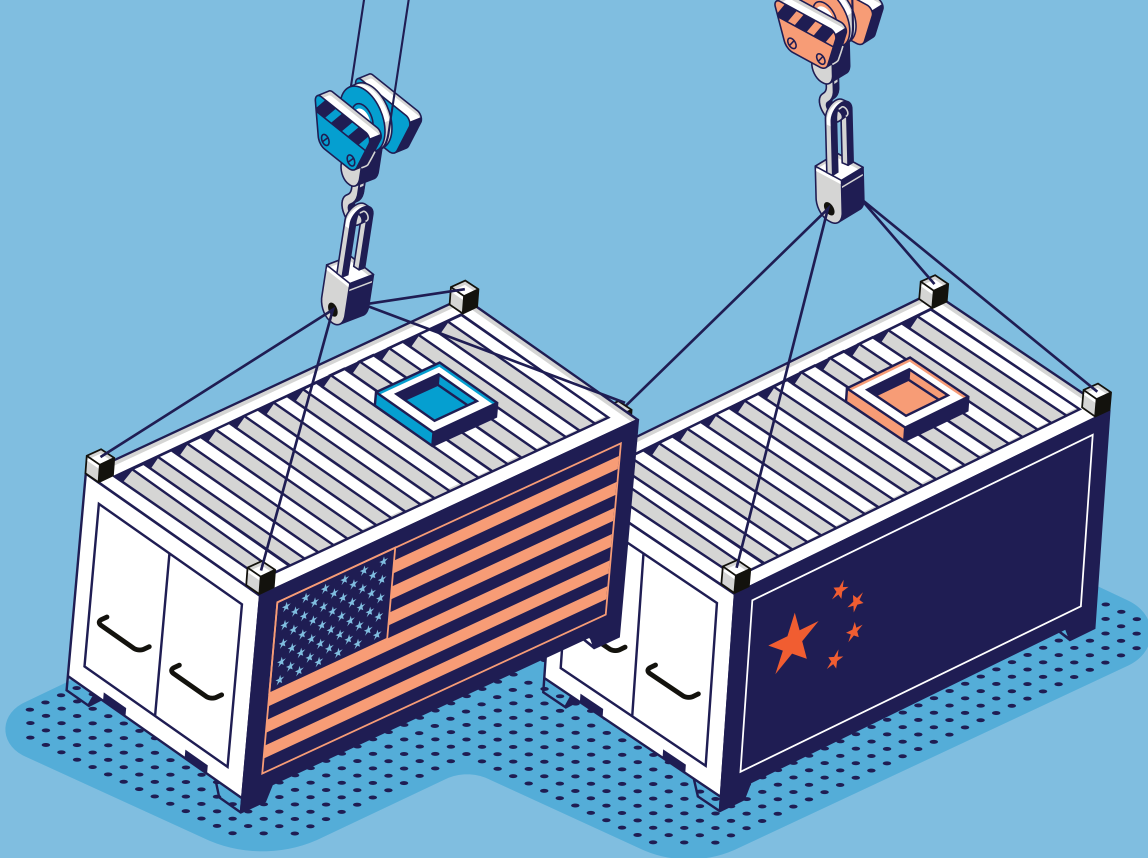




BY S.A. SWANSON



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Companies are rethinking their preferred "shoring" prefix.

For years, "offshoring" meant minimizing costs and maximizing profit. Then trade tensions and tariffs heightened supply chain anxieties—which were in turn exacerbated by pandemic disruptions.

Combined, those factors have prompted U.S. companies to consider bringing parts of their supply chains home, a process known as reshoring. They've also spurred more discussion about nearshoring, which places suppliers in neighboring countries, like Mexico. Both moves reflect companies' reluctance to depend on suppliers an ocean away.

For manufacturers and their investors, reshoring is not a new idea, but problems caused by COVID-19 have renewed—and amplified—their supply chain concerns. As companies strike a balance between domestic suppliers and low-cost countries, some are questioning the emphasis on reducing cost, at the expense of mitigating risk. Although price still matters, reliability has become a bigger differentiator, and it's generating new business for some U.S. manufacturers.

TRADING PLACES

At Incline Equity Partners, a private equity firm headquartered in Pittsburgh, reshoring and nearshoring discussions began about three years ago. The pandemic added to Incline's supply chain concerns—the firm was already "increasingly nervous" about U.S. relations with China, says Jack Glover, managing partner at Incline. "As the owner of these businesses, we want to have control over our supply chain. Our customers feel the same way," he says, noting that many of Incline's portfolio companies sell to large U.S.-based customers.

Although trade tensions increased companies' focus on supply chain risks, the pandemic forced them to rethink their solutions. That's what Larry Naughton, a corporate attorney at law firm Mintz, has observed while working with private equity firms and other investors. As the U.S.-China trade war heated up, companies considered moving their supply chains from China to other Asian countries with good trade relations. With COVID-19, says Naughton, that analysis prompted business leaders to ask themselves, "OK, we don't want to trade with a key supplier that's on the

other side of any ocean. Can we find one in the United States?"

At Fifth Third Bank, Chief Investment Strategist Jeff Korzenik sees a resurgence in reshoring discussions among middle-market manufacturers. "We've been talking about [reshoring] for a decade, but the interest level today is much higher than it has been the last 10 years," he says.

TURNING THE TIDE

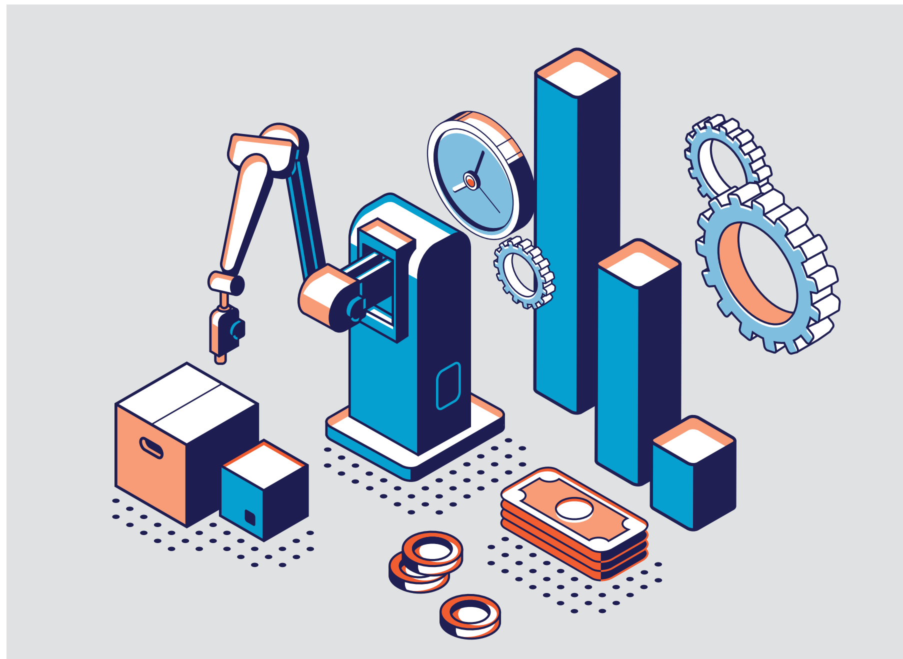
Incline is among the firms translating that interest into action as it helps one of its portfolio companies, a manufacturer of electrical products, shift production from 100% in China to a minimum of 50% in Mexico.

"The reason we went to China in the first place was to be more cost-effective," Glover says. Now the company has other costs to assess—like tariffs, potential supply disruptions and working capital considerations. Glover notes that by the time orders from China leave the harbor, the portfolio company has paid for 100% of the shipment—and then doesn't receive it for 30 or 45 days. "So we have all that money tied up," he says. "With Mexico, because we're closer, we don't actually have to spend as much money up front. Then rather than have the stuff out there for 45 days, we send them the money, it ships, and we get it two or three days later."

Incline started thinking about moving the portfolio company away from China a few years ago and began working on that process in 2019. Glover would like to see the shift to Mexico happen "yesterday," but it will likely be complete by the end of this year.

He expects the total costs related to manufacturing will be similar to those in China. "They could be 3% to 5% higher nearshored in Mexico than they are in China. But we don't expect that we're going to have the tariff issue. That's the first thing," Glover says. "Secondly, because it's significantly closer, you don't have 30 days on the water, so you need less working capital."

Preserving working capital has become critical amid the uncertainty caused by COVID-19. For many businesses with overseas suppliers, the pandemic also has interfered with their ability to fulfill domestic orders, creating an advantage for those able to manufacture products closer to their customers.



"AS THE OWNER OF THESE BUSINESSES, WE WANT TO HAVE CONTROL OVER OUR SUPPLY CHAIN. OUR CUSTOMERS FEEL THE SAME WAY."

JACK GLOVER
Managing Partner, Incline Equity Partners

Ethan Klemperer at Monomoy Capital Partners, a private equity firm based in New York City, says many businesses are seeking a balance of domestic and low-cost country suppliers—a trend that predates COVID, but that has picked up since its onset.

“SUPPLY CHAIN CONCERNS ARE DRIVING COMPANIES TO, AT A MINIMUM, REVIEW THE FEASIBILITY OF RESHORING PRODUCT.”

CLINT BUCHOLZ
General Manager, GLE Precision

Klemperer, Monomoy’s senior operating executive and head of the operating team, points to a consumer product manufacturer in Monomoy’s portfolio that experienced double-digit revenue increases (year-over-year) for June and July. Because that company has manufacturing facilities in the U.S. and China, it’s been able to meet demand for its products by expanding capacity at its U.S. facility, while its competitors struggled to keep up because most of their production was overseas, Klemperer says.

Monomoy worked with the management team to develop a more efficient factory layout and production lines, and then spent the next six months implementing the plan. This included targeted SKU (product) reduction, which allowed the U.S. facility to group similar, low-volume products together in one plant. Previously, the products had occupied sections of two plants. “We were then able to take the empty buildings and ramp up production of our core products,” Klemperer says. Those changes helped the company increase production capacity by more than 40% in less than a year. Automation also played a role, says Klemperer. He expects the company will add even more automation to expand capacity further.

PRESCRIPTION FOR RESHORING

Although interest in shifting to North American suppliers is creating new business for some companies, the transition isn't seamless. Supply chain relocation is a slow process—like "poking at a whale with a pencil," says Fifth Third's Korzenik. The planning takes time, and it requires addressing challenges posed by the North American market.

GLE Precision, a manufacturer based in Bridgeport, Michigan, is among the companies that are beginning to benefit from the shift toward American manufacturing, even as it works to manage the higher costs associated with U.S. production.

In August, the company was finalizing the reshoring of a medical project involving ejector pins used to form insulin syringes. Clint Bucholz, GLE's general manager, says he believes the project was previously manufactured in China.

Although that was the company's only reshoring project at press time, Bucholz sees possibilities for many more, based on conversations he's had with current and potential customers. "Supply chain concerns are driving companies to, at a minimum, review the feasibility of reshoring product," he says.

For GLE, which is owned by private equity firm Colfax Creek, customer order sizes range from a single component for research and development, to 20,000 units a year for a "big job," Bucholz says.

In a typical year, GLE would have about two to four possibilities for "step increase projects," which Bucholz describes as projects that would increase GLE's overall business by 15% to 100%, and worth anywhere from $1 million to more than $10 million. "Since COVID, we have seen three to four times this rate, year to date … we've got just such an explosion of these opportunities," he says.

Yet relatively high wages in the U.S. can make it difficult to compete against suppliers in other countries. To help control costs, GLE has turned to automation technology. That reflects a wider trend in U.S. manufacturing, particularly as automation becomes cheaper to implement. Bucholz notes that seven or eight years ago, it could cost around $75,000 to put a robotic arm on a machine—now it might cost about $35,000.

He says that a large-scale shift to U.S. suppliers won't be possible unless another challenge is addressed, too: raw materials. "If you reshore the manufacturing, but a company still has to get their raw material to win those jobs from offshore, it still doesn't quite get you there," he says, noting that the cost of U.S. raw materials is still quite high. Says Bucholz: "That plays a heavy part in success in truly reshoring … America needs to develop our raw materials network."

Enhanced Healthcare Partners (EHP), a private equity firm headquartered in New York City, is doing its part to improve access to raw materials for pharmaceutical manufacturing. Specifically, the firm is looking for investment opportunities in U.S.-based makers of APIs (or active pharmaceutical ingredients) used in prescription drugs.

> "WE'VE BEEN TALKING ABOUT [RESHORING] FOR A DECADE, BUT THE INTEREST LEVEL TODAY IS MUCH HIGHER THAN IT HAS BEEN THE LAST 10 YEARS."
>
> JEFF KORZENIK
> Chief Investment Strategist, Fifth Third Bank

Most API suppliers have been located overseas historically, but EHP believes there will be increasing demand to produce these components closer to home, after the pandemic revealed the supply chain disruption that can occur when countries limit exports. As of August 2019, 72% of the manufacturing facilities making APIs to supply the U.S. market were based outside the United States (including 13% in China and 18% in India), according to the Food and Drug Administration.

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"I THINK THE NEEDLE MOVED, MAYBE NOT IN A GAME-CHANGING DIRECTION, BUT A LITTLE BIT MORE TOWARD RESILIENCY OF 'LET'S MAKE SURE THAT THE SUPPLY CHAIN IS GOING TO REMAIN INTACT.'"

LARRY NAUGHTON
Corporate Attorney, Mintz

EHP is three years into a five-year plan to invest over $100 million into capacity expansion. Part of that money is for API reshoring investment, but most of it will benefit the three pharmaceutical manufacturers in its portfolio: SCA, Aphena and PAI.

Matt Thompson, partner at EHP, says the firm has always believed that quality would be a differentiator in the highly regulated pharma manufacturing world. That means a high standard for the pharmaceutical products themselves, as well as reliable access to those products through stable supply chains. The customers for EHP's manufacturing companies—mainly hospitals and doctors' offices—have always been concerned about supply chain issues, and the pandemic has amplified their fears.

To reinforce supply chain security, EHP's portfolio company PAI, which manufactures and markets generic oral liquid pharmaceuticals, started a safety stock initiative last year. The company now holds 12 weeks of additional stock on hand for each SKU, and six months' worth of API. That's a "meaningful increase" compared with the stock and active ingredients the company kept on hand before, Thompson says, adding that customers have appreciated the reliable access to liquid medications.

In recent months, Mintz's Larry Naughton has seen other companies reconsider their approach to "just-in-time" inventory. Rather than trying to maximize margins by keeping minimal supply on hand, he says businesses are now thinking, "Maybe we do need to keep a little extra inventory on hand. We can't be prepared for a nine-month shutdown on our supplier, but what if the supplier is shut down for three weeks?"

As U.S. pharmaceutical businesses look for domestic partners, Thompson says EHP's portfolio company Aphena, a pharmaceutical packaging and manufacturing services provider, is seeing more business inquiries, and the company plans to add jobs. In Eaton, Maryland, Aphena has a 110,000 square-foot facility and will be adding a 54,000 square-foot facility adjacent to its existing location. It's slated for completion by December. The Eaton location currently employs 150 full-time workers and plans to add an additional 100 jobs over the next two years.

Aphena's three Tennessee locations will add about half-a-million square feet of production capacity, slated for completion in January. The Tennessee locations currently have 340 employees and are projected to add another 50 in the next eight to 12 months.

STAYING FLEXIBLE

Companies have always made trade-offs when managing their supply chains, either to minimize cost or maximize reliability. Some observers see the events of 2020 shifting that dynamic.

"I think the needle moved, maybe not in a game-changing direction, but a little bit more toward resiliency of 'let's make sure that the supply chain is going to remain intact,'" Naughton says.

It's important to stay flexible, because today's supply chain risk may be tomorrow's asset. Three years ago, when Monomoy acquired a manufacturer with critical operations in Mexico, that location was considered a key risk. "Now that is one of its best assets, as most of its competitors manufactured in China and are having to deal with tariffs and freight surcharges," Klemperer says.

At Incline Equity, COVID-19 has heightened awareness of supply chain diversity as well as country of origin, Glover says. "One of our big issues now is, we look at country concentration for vendors," he says. "Ten years ago, I will tell you this, we were not concerned about a company that was manufacturing all of its products in China. We are now."

Glover notes that China is only one example. The firm sees risk in having all key suppliers in one country, whether that's Vietnam, Cambodia or India. Such a scenario would spark caution around a potential investment, he says.

It would concern Glover and his colleagues even more if a manufacturer had a single supplier for a particular component. "Our next question would be, 'Okay, is it just one vendor, or are there a dozen?' If there's a dozen, we feel better," he says. Having multiple vendors shows a component can be produced elsewhere if needed. But a single vendor may have a specialized process that's hard to reproduce—which makes it difficult to shift component sourcing to a different region.

"RIGHT NOW, WE'RE IN ONE OF THE CYCLES WHERE PEOPLE SAY, 'YOU KNOW WHAT? IT'S WORTH IT TO PAY A LITTLE BIT EXTRA TO HAVE THE BALANCED SUPPLY CHAIN.' IT'S ABOUT BUILDING AN ORGANIZATION THAT CAN REACT TO CHANGES IN THE MARKETPLACE."

ETHAN KLEMPERER
Senior Operating Executive, Monomoy Capital Partners

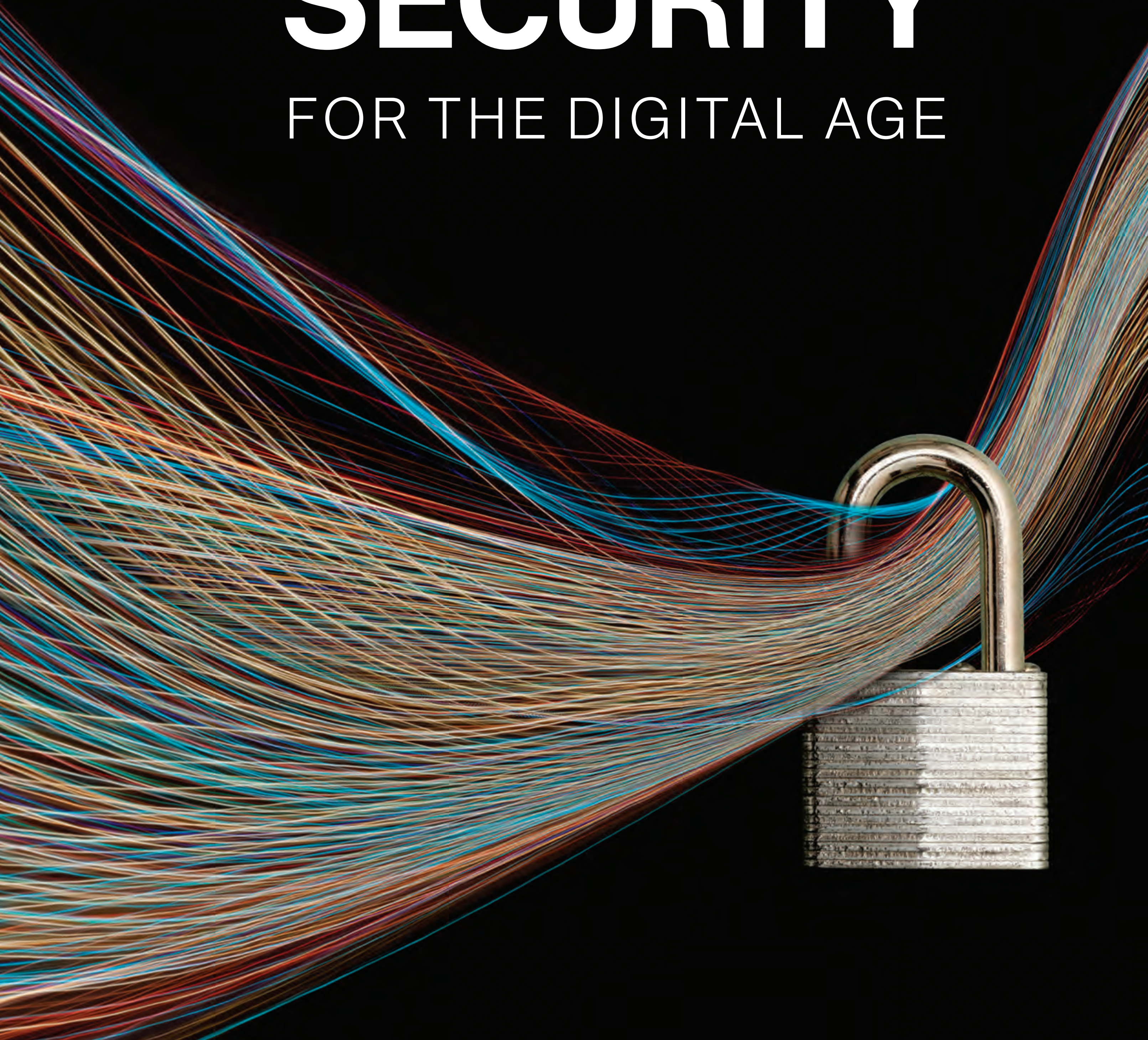
Monomoy's Klemperer notes that companies continue to move back and forth between prioritizing a diversified supply chain, or saving a little money by giving a huge chunk of volume to a sole supplier. "Right now, we're in one of the cycles where people say, 'You know what? It's worth it to pay a little bit extra to have the balanced supply chain.' It's about building an organization that can react to changes in the marketplace," he says. "Because you know there are going to be changes. You just don't know what they're going to be." //

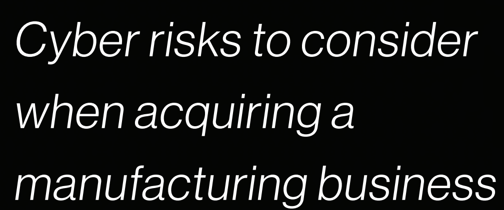
S.A. Swanson is a contributing editor for *Middle Market Growth.*

RETOOLING

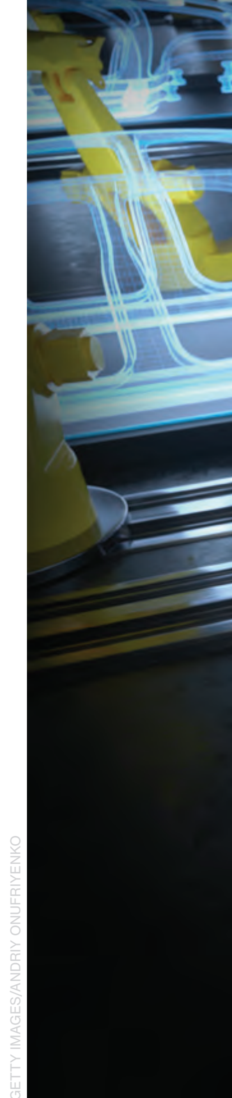
FACTORY SECURITY

FOR THE DIGITAL AGE





Cyber risks to consider when acquiring a manufacturing business



GETTY IMAGES/ANDRIY ONUFRIYENKO

BY ANNEMARIE MANNION

When Marriott International, one of the world's largest hotel chains, discovered a data breach in 2018, following the acquisition of another hotel chain, it was a massive blow for the company. As a result of the hack, the credit card numbers, addresses, passport information and other sensitive details for up to 500 million guests had been compromised.

The breach exemplified a challenge from which businesses across industries can learn: Whether you are buying or selling, it's paramount to consider cybersecurity during mergers and acquisitions.

An investigation of the Marriott incident revealed that one of the largest breaches ever of consumer data had not occurred overnight. It was traced back as far as 2014, two years before Marriott acquired the Starwood network, a family of hotels and resorts whose guest reservation database had been the victim of unauthorized access.

"WHEN I THINK OF MANUFACTURING COMPANIES AND CYBERSECURITY, I WORRY THAT SOMEONE COULD HACK INTO THEIR SYSTEM AND DISCOVER THEIR TRADE SECRETS OR THEIR FORMULAS, OR SHUT DOWN THEIR PLANT OPERATIONS."

KAREN HERMANN
Partner, Venable LLP

The large volume of personal details stolen through the Marriott breach made headlines, yet consumer-facing enterprises aren't the only ones targeted by cyber criminals. Vulnerabilities in manufacturing businesses are particularly acute, despite attracting less mainstream attention. If unaddressed, legacy cybersecurity issues can cost their future owners dearly.

"When I think of manufacturing companies and cybersecurity, I worry that someone could hack into their system and discover their trade secrets or their formulas, or shut down their plant operations," says Karen Hermann, a partner focusing on M&A and corporate transactions at law firm Venable LLP. "There are all kinds of things bad actors can do."

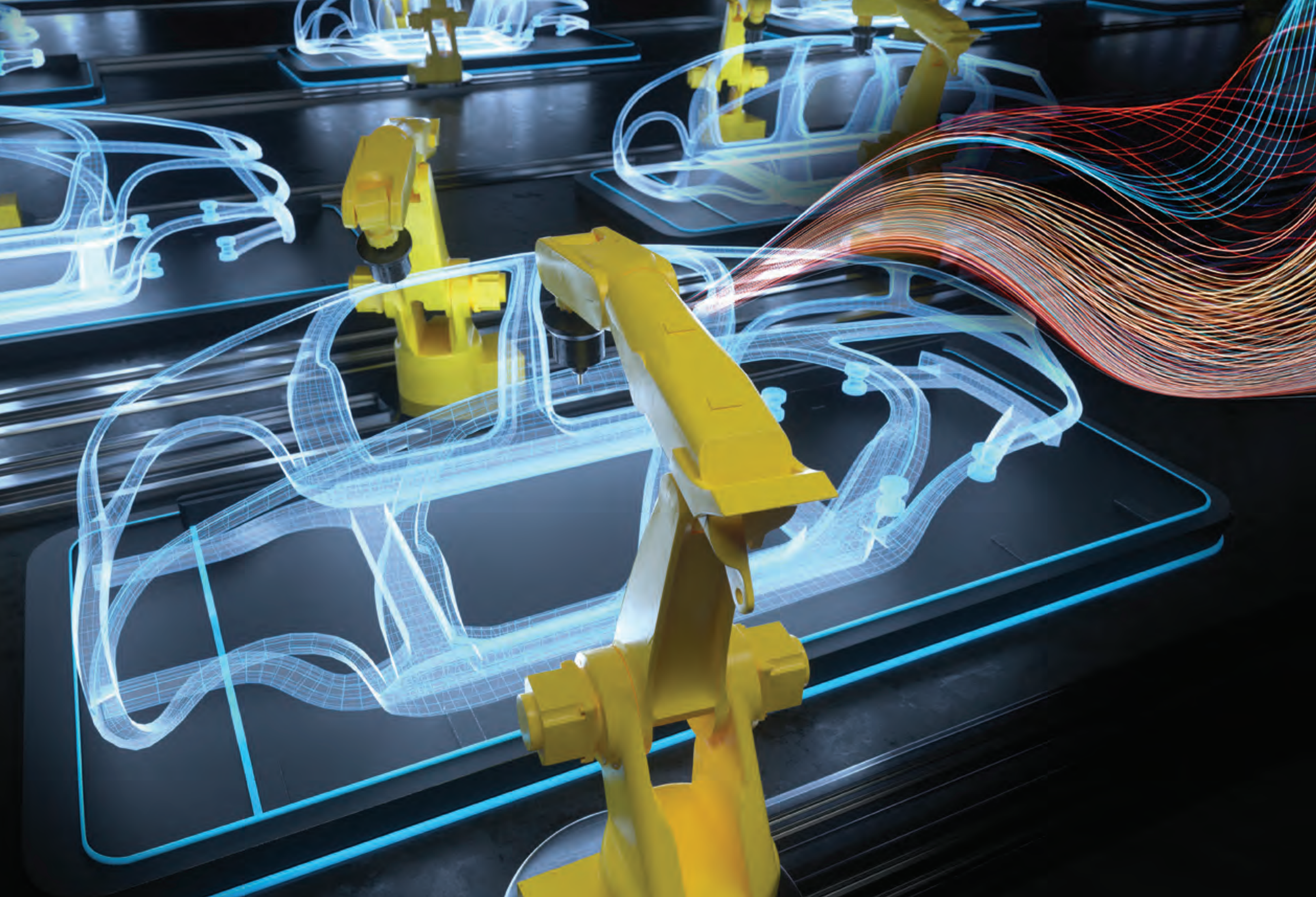
Experts say it is also common for midsize manufacturers to have outdated computer or control systems.

"They have systems that are valuable for monitoring the efficiency of production, but many were implemented years ago, before modern security techniques were in place, and they're not protected like a laptop would be," says Matt Dauphinais, senior manager of mergers and acquisitions for West Monroe Partners, a national consulting firm.

"They're also not what we call 'segmented' within a network," he adds. "If you access the device itself, you have subsequent access to all the other devices that it is connected to. In older setups, it can be a main weak point."

Tom Wojcinski, director at Wipfli LLP, an accounting and business consulting firm, frequently encounters clients who know what they want to protect within their company, yet they do not have formal risk-management programs in place.

"In the midmarket, at the ownership level, there's an informal or ad hoc understanding of 'Hey, this is what I'm concerned about,'" he says. "But it's more of a gut-level understanding of 'Hey, this is what I'm trying to protect. Did I do a good job?'"



Too often, cybersecurity doesn't become top of mind until it's too late.

"If they haven't had a problem, it's not a priority," he says. "And it doesn't become a problem until they've been burned in a ransomware attack or other hack."

Unlike financial companies, manufacturers' efforts to protect data are not highly regulated.

"There are no regulatory drivers that say you need to do this to protect your customers' assets or your customers' information," Wojcinski says.

DEALING WITH CYBER RISK

As Marriott learned after buying Starwood, an acquisition can introduce cybersecurity risks and liabilities for a buyer. The outdated security systems and lack of formal risk-management programs at many midsize manufacturers mean acquirers should tread carefully.

Among the concerns that need to be considered during an M&A transaction is the possibility of a post-sale data breach, Hermann says.

"I guess the worst thing that could happen is after closing, a buyer discovers a data breach you didn't tell them about and then, all of a sudden, you're on the hook to give them back a big chunk of the purchase price for an indemnification," she says.

Despite the threats posed to businesses, Dauphinais says cybersecurity does not receive as much focus as it should during M&A.

"I think there's a lack of understanding of what the risks really are," he says. "You could have a ransomware event and that could be just as impactful, if not more damaging, than a couple quarters of missed financial projections."

While inadequate cybersecurity protocols alone will rarely sink a deal to acquire a company, they will potentially impact the purchase price or terms. »

GETTY IMAGES/QI YANG

“THE BEST HACKERS DON’T HACK COMPUTERS. THEY HACK PEOPLE.”

TOM WOJCINSKI
Director, Wipfli LLP

“If you feel a company has been lax in any area of preparation—their financial statements aren’t as robust as they could be, or they don’t have cyber insurance or they don’t have good benefits plans—all those things weigh into the price of the deal,” Hermann says.

A company that is the target of a purchase should be able to demonstrate good governance overall.

“Make sure you have good policies in place,” Hermann says. “Make sure your employees are being trained and you have a good data protection policy on the website. Make sure you know what data you collect, how you store it and who has access to it. Change your passwords every 90 days.”

One way for a company to identify its cybersecurity weaknesses is to hire an outside firm to do an assessment.

“If you really want to put your best foot forward, hire a third-party investigation to do a phishing test or a penetration test,” Hermann says.

Even if a gap is revealed, “at least you’d look like you’re aware of it,” she adds.

Paul Cotter, senior security architect for West Monroe Partners, says companies that discover security weaknesses should develop plans for addressing them.

“What we generally advise is that if you’re looking to sell a company, you want to make sure that if you are aware of a gap, you demonstrate that you know about it and that you have a plan to address it, either short-term or long-term,” Cotter says. “Or be ready to establish that the gap is not as critical as perhaps some other issues.”

For a company that’s looking to sell and has been compromised, Wojcinski wants to see documentation of what they’ve done to correct the issue.

“If you got cracked wide open, and you had a compromise, I’d want to see a follow-up to show me that it’s been fixed,” he says.

CLOSING THE GAPS

When working with a buyer, Wojcinski says his job is to predict any post-close, unexpected costs. One area that can be costly is ensuring software and servers are up to date with the latest patches.

He cites Windows 7, which is no longer supported by Microsoft, as an example.

“You could have highly important manufacturing systems that are dependent on vulnerable software that can’t be patched,” he says. “A

buyer should know that they are buying vulnerable infrastructure that can't be updated. And they need to think through, 'Am I prepared to have this machine go offline in an attack and not be able to recover it?'"

Wojcinski and other experts say companies should consider purchasing cybersecurity policies and know their limits and exclusions. He notes these policies can be tailored to the particular risks a company faces.

Another area to look at is employee training.

"The best hackers don't hack computers. They hack people," Wojcinski says. "It is way easier for me to trick you into giving me your password so I can come back into your system using your credentials rather than figure out how to circumvent the technical safeguards that are already there."

He adds that training employees to recognize security threats isn't enough; companies must promote a culture that encourages them to ask questions.

A common security threat is a hacker who sends an email pretending to be a trusted person within a company.

"I want to know if there is a culture in the company where it's OK for an employee to question one of those messages and ask, 'Is the director of finance really asking me to do this?'" Wojcinski says.

"HOLES THAT DIDN'T EXIST BEFORE"

Another area where a prospective buyer should focus is on the products a company sells, particularly as artificial intelligence, internet-enabled devices and other technologies become more prevalent.

"I worry about whether a company I'm buying has caused a third party to have a problem," Hermann says. "If I'm buying a company that is selling iPhone speakers but is not designing them appropriately to not be hacked, then that could result in a class-action lawsuit."

During the due diligence phase of a potential acquisition or merger, Hermann says bankers and lawyers hired as advisers should be asking a lot of questions about cybersecurity, as well as other areas.

She wants to understand any potential liabilities a company's products may have.

"I'm going to be asking a lot of questions about what is referred to as 'security by design,'" she says. "How is the company designing their products? Are the products they are putting out there safe or are they vulnerable to an attack?"

Events that are well beyond a company's control—the COVID-19 pandemic, for instance—also can affect cybersecurity.

Cotter says employers rushed during the pandemic to enable employees to work at home, which has created security gaps.

"They didn't do as much research or take the time to necessarily acquire all the right security tools and hardware and everything else," he says. "A lot of companies created new holes that didn't exist before."

As companies seek to improve their cybersecurity protections, Hermann says they also need to think about how they would justify their protections if they ever end up in court.

She recommends that manufacturers make their companies as secure as they can and adhere to industry standards. In the event a case goes to court, the business will be in a strong position to say to the judge or class-action litigators, "I got hacked. But I did all these things that were up to industry standards, the bad guys were just smarter than the industry," Hermann says.

Planning ahead can help shield a company from future litigation as well as improve its prospects for acquisition. Knowing its cybersecurity weaknesses and addressing them can be key for a seller to get the best deal possible during the M&A process.

Awareness and follow-up are key.

"If somebody comes into a deal and is self-aware, and has a plan for addressing security gaps, that puts them in a much stronger position than if they're just unaware and are completely oblivious to what the issues are," Cotter says. //

Annemarie Mannion is a former reporter for the *Chicago Tribune* and freelance writer who covers business.

DIXON HUGHES GOODMAN LLP

For Health Care M&A, Turn to a Specialist

DHG's health care focus makes it a trusted adviser for private equity

The business of buying and selling health care companies has never been an easy one—add a global pandemic and an economic recession, and it's no surprise that transactions have become downright difficult. However, private equity professionals do not have to go through the process alone. Trusted advisers can help deal professionals navigate even the most intricate parts of transacting in this highly regulated space. Even more helpful is when a private equity firm can work with a trusted adviser that has in-depth industry knowledge and can be a one-stop resource, versus having to rely on a cadre of partners.

Enter Dixon Hughes Goodman LLP (DHG), a national advisory firm with more than 2,000 professionals, including a dedicated team servicing the middle-market private equity industry, with a specialization in the health care sector. "Our expertise in both private equity and health care allows us to offer a unique value proposition to our clients," says Kevin Locke, managing principal of DHG Healthcare. "We look at the deal from both a private equity perspective and a health care perspective, ensuring a thoughtful and comprehensive approach to the transaction."

"We enjoy being very collaborative and having open dialogue with our clients about their needs, and then addressing those needs and helping them with other challenges," adds Scott Berte, a managing partner with DHG. "We are passionate about helping our clients achieve their goals and we will keep working hard for our clients to get them what they need to be successful."

These characteristics, in addition to a seamless operating philosophy, have made DHG the chosen adviser for many middle-market private equity investors, including One Equity Partners, a New York-based firm with more than $4 billion in assets under management. DHG has worked closely with a health care business in One Equity's portfolio, helping it grow through M&A and navigate the regulatory complexities of its multistate operation.

In 2016, One Equity purchased Simplura Health Group. Founded more than 60 years ago in Lynbrook,

"WE ENJOY BEING VERY COLLABORATIVE AND HAVING OPEN DIALOGUE WITH OUR CLIENTS ABOUT THEIR NEEDS, AND THEN ADDRESSING THOSE NEEDS AND HELPING THEM WITH OTHER CHALLENGES."

SCOTT BERTE
Managing Partner, DHG

New York, Simplura has since grown to become one of the largest home health care agencies. Under One Equity's ownership, Simplura has acquired seven health care companies and now operates in New York, New Jersey, Florida, Pennsylvania, West Virginia and Massachusetts.

As Simplura expanded, One Equity knew it needed to team with an advisory firm with a deep understanding of the health care industry that could help the company navigate compliance issues in different markets across the nation and offer top quality service. It chose DHG. "With our broad and deep health care expertise, we're able to advise our clients through the regulatory, financial, operational and strategic issues that emerge through the life cycle of any transaction. Our goal is to provide value before, during and after the transaction so our clients can focus on growing their business and executing their strategy," Locke says.

"The DHG relationship started with audit, assurance and health care compliance services," says Brad Coppens, a managing director with One Equity. "The relationship grew into transaction services and support for all our add-on acquisitions. They have done a great job helping us manage all our add-on acquisitions and beyond."

Simplura's needs evolved as it grew, and DHG was able to adjust its client service accordingly.

"We were doing Simplura's audit and assurance work and then moved into transaction work as they started to become fairly acquisitive," says Jay Stine, a partner with DHG. "We wanted to work with Simplura, help them achieve their goals and be an adviser regardless of deal size." DHG was able to tailor its scope of work so that both parties were comfortable, and for several years, the firm has worked side-by-side with Simplura on both large and small add-on transactions. "No matter what size the transaction, the quality of our work is the same and our findings are communicated in the same way," Stine adds.

Although DHG's reach is national, it offers personalized attention to its clients, a rare and differentiating quality that One Equity appreciates.

Illustrations by Joel Kimmel

DHG HEALTH CARE SERVICES AT A GLANCE

In response to the evolving U.S. health care market, DHG established a dedicated health care practice to inform, guide and support clients so their organizations can realize their long-term potential.

Year DHG Healthcare was founded: 2013

Goal: To guide clients along their journey toward risk capability

Number of dedicated industry professionals: 300

Health care services offered: Management consulting, regulatory consulting, transaction advisory services, health care audit and health care tax

"It can be difficult for larger firms to have a local feel and personal connection. For us to be able to get corporate advice and translate it to all the subsidiaries in a meaningful way can be a challenge. DHG does that exceptionally well," Coppens says. "They really work across all our different groups to communicate and help, and they still stay within budget."

HEALTH CARE ALL THE TIME

"Health care is a complex industry where deep expertise matters. It requires an understanding of the regulatory environment, third-party payor system, revenue dynamics, payment mechanisms, operational challenges and market opportunities, all of which are constantly changing. Our understanding of those evolving dynamics across the health care industry can be a significant advantage to our clients," Locke says.

DHG's industry focus on health care gives the firm an advantage over generalist advisory firms.

"We help our clients with due diligence procedures

"NO MATTER WHAT SIZE THE TRANSACTION, THE QUALITY OF OUR WORK IS THE SAME AND OUR FINDINGS ARE COMMUNICATED IN THE SAME WAY."

JAY STINE
Partner, DHG

that not only serve financial and accounting matters but can go beyond that as to help our clients evaluate the transaction; such as, determining how quickly insurance companies will pay, validating reimbursement rates, and assessing billing and coding compliance," Stine says. "These are just some of the things that we are consistently looking at as we strive to reduce the risks for our clients and search for synergies within a transaction."

That specialized knowledge is especially critical for M&A. Unlike in many industries, the complexity of a health care transaction does not change based on deal size. Each engagement requires the same level of rigor from a transactional standpoint. "When it comes to health care, you can't cut corners. You need the same quality of service without sacrificing quality. Health care companies are extremely nuanced," Coppens says. "DHG gets that."

DHG also recognizes that a private equity firm's work is not complete after the deal closes, and it is ready to help health care investors realize the returns they need to stay in the top quartile. "When private equity firms make their first investment, they have a thesis, which can be about organic growth or acquisitions. Whatever their thesis is, we can look at the top issues and prepare that company so it's ready to be sold at the best value," Berte says. "We prepare portfolio companies for the next exit."

Some of the most common problems Berte sees with health care portfolio companies are issues with billing and coding platforms, complications with post-merger integrations, and tax preparedness. DHG works with clients to get ahead of those issues, so they do not interfere with an eventual sale. "We help owners become free of tax concerns and ready for exits," Berte says.

Ultimately, the goal is to take the burden away from private equity firms and their management teams, by providing professional advice to contribute toward the success of their businesses. "It's all about making things easier for our clients," Stine says. "We work across our teams and transfer the knowledge to our clients in a seamless process, which equates to less work and more value add for our clients." //

U.S. HEALTH CARE EVOLVES

The U.S. health care industry is undergoing a radical transition as it shifts from a fee-for-service model, to a system where value is defined by outcomes. At the same time, the players are changing, and acquirers are increasingly prioritizing efficiency, quality, outcomes transparency and access.

Successfully navigating this shift will require:

- Adept management of the physician enterprise
- Keen insight into an evolving revenue portfolio
- Skilled connection of varied payment programs to larger population health challenges
- Exceptional management of increasingly complex reimbursement and regulatory environments
- Sophisticated recognition of and responses to a variety of complex associated business risks

The Importance of a Human Capital Management Strategy

SOUND DECISIONS // Solutions to help move your portfolio forward

Randy Fisher
Strategic Marketing Manager – Marketing & Business Development, Insperity

For months, economic forecasters were anticipating the economy would take off in the fall as the COVID-19 pandemic receded, consumers reverted to natural spending patterns, and job gains increased in late spring and early summer. Those same forecasters were hoping for a "V-shaped" recovery but have since abandoned that hope for any type of quick economic recovery. But there are some tips that can help companies adapt to the new economy and reach for new levels of prosperity.

Reconnect with your people.

At the end of the day, it takes more than competitive pay and a good benefits package to retain current employees and win candidates over. A well-developed strategy and a growth-minded company culture can lead to less turnover, increased employee engagement and leadership succession strength. The value of a strong company culture will help any emerging or middle-market company prepare for their next evolution.

"WHEN COMPANIES HAVE ALIGNMENT TO THEIR CORE VALUES AND GOALS, IT BECOMES EASIER TO OVERCOME OR THRIVE IN ANY ECONOMY."

Challenging times call for smart leadership.

If your company is positioned for growth, you must develop and equip your leaders who can take the company into the future, drive the business, and sustain the culture. The organizational structure is solidified around the best employees who are ready to step up when the need arises.

Align your executive team to cascade the company's vision, strategy and goals to optimize growth, profitability and employee performance.

By defining a clear strategic direction for the future, leaders strengthen the organization's infrastructure, optimize employee performance through clear direction, and provide the tools and support that can impact the fortunes of any company. Alignment from the top down helps ensure the right people are in the right position for success.

Smart companies hire for the company, not just for the job.

When companies have alignment to their core values and goals, it becomes easier to overcome or thrive in any economy. Review your mission statement, vision and values and you will improve your profitability through a stable, engaged and committed workforce.

Utilizing these tips can help any company find predictability in a world of uncertainty. By keeping your human capital management strategies at the forefront of changes, you maximize your chances of success. //

Randy Fisher leads capital market innovation efforts at Insperity to work alongside investors and founders and overcome the HR challenges that many startups, emerging and middle-market companies face.

COVID-19's Impact on International Business

GLOBAL VIEWS // CFO survey reveals the pandemic's effects

Diane Albano
Chief Revenue Officer, Globalization Partners

The economic climate in the wake of COVID-19 is creating new challenges for international growth. To understand the impact of the pandemic, Globalization Partners and CFO Research surveyed CFOs in organizations with international expansion plans and revenues of more than $100 million. Here's what we found:

Businesses with expansion plans are undeterred. A majority of CFOs surveyed are undeterred by the impact of COVID-19 and are continuing with their international expansion plans. Forty-five percent of respondents are either currently expanding globally or are only slightly delaying their plans within the next year. Another 9% intend to expand in one year or more.

After North America, the Asia-Pacific region (excluding China) is the region most often identified as the place for new or expanded operations. Capturing market share was the most cited reason for expansion into these specific regions, followed by the desire to expand sales, diversify investments and acquire top talent.

COVID-19 is accelerating change. COVID-19 is accelerating the pace of change across organizations everywhere; 83% of respondents said they are now looking to the remote, global workforce model as a solution to the changes brought about by the pandemic.

Working remotely has become a defining feature of the crisis, with many companies allowing employees to work from home permanently. Corporations like Twitter, Facebook and others have made long-term commitments to telecommuting, while others like Amazon, Google and Salesforce are allowing employees to work from home into 2021.

Employee health and safety is a top priority. Employee health and safety is a top concern for CFOs focused on global expansion. Survey respondents cited it nearly twice as much as the other leading issues, including new business strategies, increasing revenue, and reducing organizational costs.

Third parties, banks and payroll are among the biggest challenges. Looking at other obstacles to growth, 83% of executives expressed concern about managing third parties and stakeholders in a foreign environment during business expansion. Seventy-four percent of respondents are concerned about working with foreign banks and managing international employee payroll.

Using traditional methods for international expansion is a slow process. According to the survey, 86% of CFOs say their global expansion is anticipated to take at least five months. That includes 42% who say it could take more than one year. It's perhaps not surprising respondents say that dedicating resources to global operations was the top concern for planning international expansion.

To avoid the difficulties associated with global expansion, many companies are now opting to use a Global Employer of Record to establish new international teams and revenue generation in a matter of days. This alleviates complexity, making it easy to meet ambitious business goals and replicate success in new countries.

We are finding that many businesses remain optimistic and determined that the disruption caused by COVID-19 will not stand in the way of the opportunities offered by international expansion. While resilience is a "must have" quality for any business, innovation will drive recovery and prosperity in post-COVID-19 economies. That comes from identifying where change—and yes, even expanding to new geographies—can have the greatest positive impact. //

Diane Albano has led high-performance sales teams for more than three decades and is recognized for her strategic expertise in managing complex sales and services organizations.

COVID-Era Private Credit Trends: Liquidity Covenants In, DDTLs Out

MIDMARKET TRENDS // The pandemic ushers in changes to the debt market

Abby Latour
Editorial Lead, Leveraged Commentary & Data, S&P Global Market Intelligence

A rash of covenant violations due to government-mandated shutdowns has forced lenders to reevaluate portfolio companies and rewrite covenants. As a result, new trends have taken shape in private credit during the pandemic era, according to Lincoln International, which provides mergers and acquisitions, capital advisory, restructuring and valuation services.

These trends are as follows: Restructuring experts are in. Takeovers by lenders are not. Minimum liquidity covenants are in. Leverage and fixed-charge covenants are out. Smaller revolvers and hold sizes are in. Unfunded delayed-draw term loans, or DDTLs, are out.

On the topic of liquidity covenants, private debt providers have begun temporarily installing minimum liquidity requirements to replace leverage tests, typically for six to nine months, as part of amendments after borrowers break covenants.

"Liquidity covenants were far more exceptional pre-COVID. Now they're much more mainstream," said Ronald Kahn, co-head of Lincoln's U.S. Debt Advisory and Valuations and Opinions groups.

Liquidity covenants are typically calculated as cash on hand plus revolver availability, measured monthly or quarterly. Amounts vary, depending on company size, profile and capital needs.

"Most of these companies will go back to a leverage test in Q4 2020 or Q1 2021. It buys everybody time to get some perspective on what the new normal is for a business," said Christine Tiseo, co-head of Lincoln's Debt Advisory group.

Instead of modifications, recent amendments typically offer a reprieve for near-term quarters from performance metrics linked to earnings, such as leverage and fixed-charge covenants.

"What matters is how much liquidity a company has, so the lender knows how much runway a company has before there's a problem," Kahn said.

The Bells and Whistles Are Gone

The difference between pre- and post-pandemic loan agreements lies in the "bells and whistles," which are now harder for a borrower to come by, Tiseo said.

These include large unfunded DDTL commitments with a broad list of preapproved uses, and wide open free-and-clear baskets. Today, the use of proceeds would be far more restrictive, and the facility size would be significantly smaller than before.

Another change in recent months has been increased volume of M&A financing versus refinancing. At Lincoln, the balance between acquisition financing and refinancing is usually split evenly.

"We seem to be more heavily weighted in acquisition financing, which is not what we were expecting," Tiseo said.

The deals that are closing in the private market now involve high-quality businesses that are what the firm identifies as "pandemic-proof." These new terms are stronger than "recession-proof" and "recession-resistant" buzzwords of recent years.

No Takeover Rush

Another trend among private credit providers is hiring restructuring experts to negotiate and run amendments and forbearance agreements. But taking ownership of companies has not happened in significant numbers.

"We always thought private debt lenders would act differently than banks," said Kahn. "They don't have the regulation. They don't have the bureaucracy. The mentality is similar to private equity, so they have a longer outlook." //

Abby Latour is an editorial lead for LCD, covering direct lending and the middle market.

Businesses Seek a Renewed Lease on Life

BY THE NUMBERS // Navigating leased properties is the only way to right sinking ships

Nico DePaul
Senior Managing Director, STNL Advisors

Over the past seven months, the COVID-19 pandemic has presented unprecedented challenges for operating businesses throughout the country. Companies are trying to stop the bleed of lost revenue in any way possible, while they navigate new guidelines and restrictions for running their businesses. Cutting costs is a necessity and everyone is sharing the burden.

One lever that has received significant media coverage is reducing rent burdens. This is a polarizing topic with different news articles portraying both sides—tenants and landlords—as villains. Unfortunately, the reality is that businesses are fighting to survive and need to reduce costs in order to do that. At the same time, landlords are in the same boat; they need to service their debt or live off of their rent collections. The majority of tenants affected negatively by COVID-19 have most likely reached out to their landlords for rent relief, whether that be in the form of abatement, deferment or a combination of the two. Although this is a difficult conversation to have, it is not necessarily one that requires a winner and a loser. It does not mean leaving someone happy and someone upset.

> "AS COVID-19 CONTINUES TO HAVE AN IMPACT ON BUSINESSES THROUGHOUT THE WORLD, IT HAS NEVER BEEN MORE IMPORTANT TO SECURE THE SUSTAINABILITY OF YOUR BUSINESS."

The tenant-landlord relationship does not need to be restricted to a rigid, financial transaction of paying and collecting rent, or fulfilling or not fulfilling obligations. In most instances, leases are longer term in nature and require a multi-year and sometimes multi-decade relationship. If approached correctly, tenants should be able to receive the concessions they desperately need to survive and landlords should be able to see the long-term benefit of a negotiation that can add security and value in the future.

There is certain to be emotion in these difficult conversations that can ultimately provide for unproductive negotiations and grandstanding. STNL Advisors has been working day and night on behalf of its clients since early March on achieving their goals while balancing the needs and concerns of landlords.

Since the outbreak of the coronavirus unleashed a wave of shuttering, unshuttering, re-shuttering and re-unshuttering of businesses and state economies, STNL Advisors has renegotiated more than 6,000 leases. Some of the outcomes include three-month to nine-month abatements, three-month to 12-month deferrals, and partial abatements and partial deferrals of varying terms. Other outcomes include early lease terminations, 15% to 30% long-term rental reductions, and Purchase Options and Right of First Refusals secured.

As COVID-19 continues to have an impact on businesses throughout the world, it has never been more important to secure the sustainability of your business. Unfortunately, no one is sure what the coming winter season will mean for businesses and the country. Even if you worked out a short-term fix with your landlord, it is very likely that negotiations will need to resume, as being proactive typically secures the better outcome. Formalizing a strategy today can mean being in business 12 months from now. //

Nico DePaul is the senior managing director with STNL Advisors, which provides real estate consulting services to private equity firms and their portfolio companies.

Protecting Portfolio Companies Against Black Swan Events

SOUND DECISIONS // Don't let outdated technology stand in your way

Jacob Halusic
Account Executive, Velosio

After this year, having 20/20 hindsight will mean something new. Rather than referring to the perfect vision everyone has in assessing the past, it will be used to comment on what we learned from living through the COVID-19 pandemic. So here is some 20/20 hindsight: Do not wait until a crisis to invest in technology for your portfolio companies.

Market volatility and economic uncertainty had a profound impact on dealmaking for most of 2020, leaving many private equity firms focused on creating value from their existing portfolio. Fortunately, strengthening the competitive position of portfolio companies during a recession can result in big gains. However, strengthening a competitive position is difficult when outdated technology platforms stand in the way of change.

Early in 2020, many organizations struggled to make the shift to a virtual workforce and maintain even the most basic operations. The inability to respond to the pandemic swiftly stemmed from rigid, disconnected systems ingrained with manual processes and workflows. On the other hand, companies already invested in modern cloud solutions with mobile access, scalability, integrated data and artificial intelligence were able to maintain business continuity while easily moving to the work-from-home business model.

A Real-Life 2020 Success Scenario

A supermarket goods distribution company pivoted successfully to supplying stores with critical products such as hand sanitizer, face masks and other high-demand items. This change required the company to find sources for new products and reengineer their distribution channel, all while shifting to a remote workforce.

While this change was taking place, operations and finance executives had to be mindful that, at some point, they would go back to distribution of their normal product lines, and they needed to plan accordingly. For example, financial data from 2019, based on the company's standard business model, would look very different from financial data for 2020. But a likely return to standards in 2021 would require them to take both models into consideration.

Successfully undertaking and accounting for these business model changes without disrupting revenues was only possible with flexible, agile technology in place. The technology gave executives the ability to collaborate remotely using connected, real-time assessments of financial performance, as well as access to historical pre-pandemic data. Without the right technology already in place, this distribution company would not have been able to meet new market demands.

Protect Portfolios with Strong Technology Investment

Investing in the right systems and technology is one of the most overlooked strategies for private equity firms to protect their investment in portfolio companies. With 20/20 hindsight, it's easy to see that modern, cloud-based technology not only better prepares organizations to weather future black swan events, it also positions them for innovation and progress. To learn five ways Velosio delivers for your portfolio companies, visit www.velosio.com/private-equity. Download a free e-book on making faster, smarter decisions through technology. And, when up against a crisis, it can mean the difference between new opportunities and lost profits. //

Jacob Halusic is an account executive at Velosio, a leader in the deployment of Microsoft's integrated cloud solutions for private equity firms and portfolio companies.

Pave the Way for Success in a Post-Merger Transition

SOUND DECISIONS // How to navigate the integration process

Jeff Servais
Principal, CLA

The deal is done and the signatures are dry. You've identified the target acquisition, completed due diligence, and finalized the purchase agreement. You've spent an inordinate amount of time and effort to successfully get both sides to the table. Now, there may be a natural tendency to pause, exhale and celebrate.

While private equity deals can be an exhaustive process, the post-merger integration phase is just as important. Mismanagement during this phase is one of the most common reasons mergers or acquisitions fail. Be sure to understand how to navigate the post-merger integration for long-term success.

Overcome a Lack of Preparation

Frequently, new owners are ill-prepared ahead of a business transition. It's possible the previous owner left unreliable operational and financial infrastructures in place, which could bring additional challenges. Even if infrastructure is adequate, the previous owner may no longer be around to answer questions. Lack of clarity on infrastructure, combined with a gap in legacy knowledge, can also impact your recently acquired organization.

Ideally, these pain points are identified during due diligence. If not, you must address these hurdles after the transition is complete. Every acquisition is different and there is no one-size-fits-all approach for a successful post-merger transition. Be sure to seek experienced guidance during the process. You can also leverage the same people in both the due diligence and post-acquisition phases since they have seen the organization's shortcomings firsthand and can help identify ways to move forward.

Identify Transitional Needs

Post-merger integration often brings several new projects, each with its own needs and timelines. For example, you may find a need to outsource the payroll and benefits mechanisms or hire a new bookkeeper. Realize that it may be a long and arduous process to work out costs, identify enterprise resource planning software, and accommodate staffing.

These hard-to-calculate needs can make the transition challenging. However, once you identify them, you can determine realistic solutions. Although you could hire staff and handle any challenges internally, doing so could be expensive in the long run.

Plenty of individuals or organizations can offer guidance and consulting, but you should first determine whether these solutions are right for you. Consider assistance from a third party who wants to see the organization succeed in your vision—not someone who wants to integrate their products or services. That assistance should come from a partner who can help navigate the heavy lifting of the transition and then step aside to leave you confidently in control. Look for someone with experience dealing in the small-to-midsize market, and with a track record of working with founder-owned company transitions.

The right partner can help successfully navigate the post-merger integration. Once that process is complete, it's finally time to celebrate. //

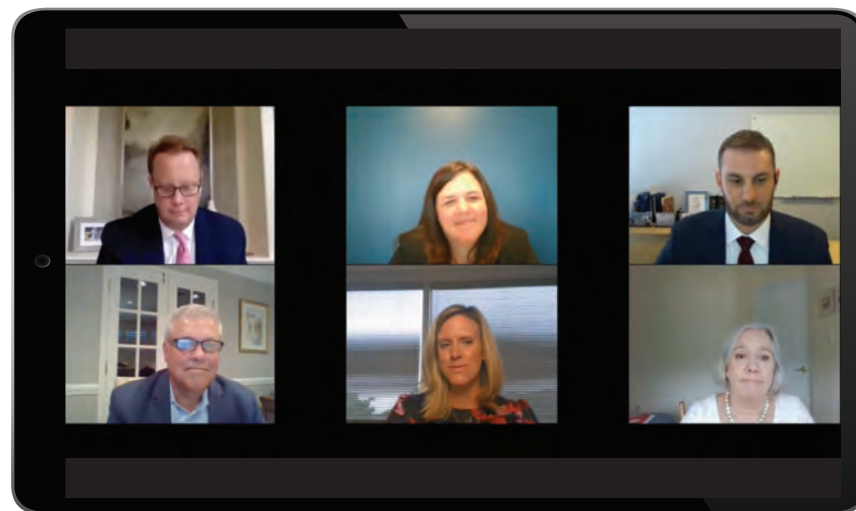
Jeff Servais has over 15 years of public accounting experience and is a principal in charge of the Transaction Services practice for CLA (CliftonLarsonAllen LLP), where he works with a variety of clients from development stage to private multinational companies. CLA has extensive experience with small to midmarket mergers and can help ease the pain of a post-merger integration with its customized approach.

ACG chapters have used the pause of in-person meetings to offer innovative programming and networking opportunities online. In some cases, they've collaborated on virtual programs with other chapters, in order to bring together middle-market deal-makers from across the globe. The shift to a virtual environment has created an opportunity for chapters to broaden their geographic reach and convene ACG members who might not otherwise have met.

Below are a few recent ACG-hosted online events. Check out acg.org/events to see a full list of webinars, networking events and panel sessions, and take advantage of the full breadth of ACG content, now more accessible than ever.

ACG TORONTO

ACG Toronto hosted a webinar series on family offices and the role they play in the middle-market investment sector. One webinar focused on how family offices source and assess deals compared with other investors and capital providers. The series was sponsored by Aird & Berlis and featured speakers from Hyatt Family Office, PHF Capital Inc., White Owl Limited, and Family 2 Family Capital Connection.



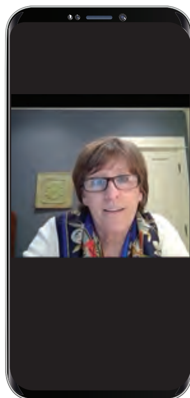
ACG NATIONAL CAPITAL

ACG National Capital hosted its 18th Annual Corporate Growth Awards gala, this time in a virtual format. The awards celebrated the accomplishments of the Washington, D.C., metro region's corporate growth executives, investors and transaction teams.

ACG NEW YORK

Appraisal, legal and private equity experts discussed the ways valuations are changing during one of ACG New York's webinars. Moderated by Frank Marcucci, the national director of business development for Corporate Valuation Advisors, Inc., the panel also featured Jim Volkman, Corporate Valuation Advisors; Lori Smith, White & Williams LLP; and Don McDonough, JLL Partners.

> "MOST OF MY CLIENTS SAY WITH PRETTY GOOD CERTAINTY THEY'LL LOSE MONEY OVER THE NEXT 12-18 MONTHS, BUT THEY'RE MUCH LESS CERTAIN ABOUT WHEN THEY'LL RETURN TO PROFITABILITY—AND WHEN THEY'LL RETURN TO PRE-PANDEMIC PROFITABILITY."
>
> JIM VOLKMAN
> Managing Director of Financial Valuation Services at Corporate Valuation Advisors, describing the evolving trends in valuations during a panel session hosted by ACG New York



ACG ST. LOUIS

ACG St. Louis hosted a webinar session on the role of middle-market companies in supporting philanthropy. The session featured two philanthropic leaders in the St. Louis area – Amelia Bond, CEO of the St. Louis Community Foundation, and Tracy Hart, CEO of Tarlton Construction. They discussed their role in guiding nonprofit organizations to success and how the business community contributes to resiliency in the St. Louis area.

ACG BOSTON

ACG Boston launched its "Getting Deals Done in the New Normal" virtual lecture series throughout the summer, which provided guidance on changes to the M&A process brought on by the COVID-19 pandemic, and fostered discussion about how dealmaking will look different in the months ahead. Topics included deal sourcing, go-to-market strategies and valuation, diligence and closing.

ACG AUSTIN/SAN ANTONIO, ACG COLUMBUS & ACG DETROIT

ACG chapters from Austin/San Antonio, Columbus and Detroit teamed up to host a virtual panel session on what the M&A market will look like as the world adjusts amid the coronavirus pandemic. Sponsored by law firm Dykema, the panel featured analysis from Joseph Tracy, executive vice president of the Federal Reserve Bank of Dallas. Citing figures from the Fed and other agencies, Tracy showed the economy began to recover in the spring as infections declined, but then economic conditions worsened when COVID cases began to rise again over the summer.

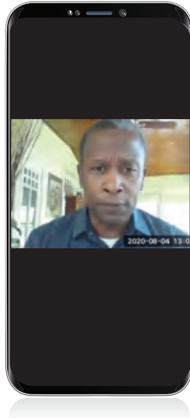
> “RECOVERY REALLY WILL DEPEND, IN SOME PART, ON WHAT IS THE PATH IN TERMS OF OUR ABILITY TO GET THESE INFECTIONS TRENDING BACK DOWN.”
>
> JOSEPH TRACY
> Executive Vice President, Federal Reserve Bank of Dallas, on the interconnectedness of economic performance and the spread of COVID-19

ACG CINCINNATI, ACG KENTUCKY & ACG TENNESSEE

Co-produced by ACG Kentucky, ACG Cincinnati and ACG Tennessee, the webinar series “A Tale of Three Cities” featured three panelists who discussed opportunities, challenges and insights they saw from their local midsize markets – Cincinnati, Louisville and Nashville – and beyond. Moderated by Brad Smith, MCM CPAs & Advisors, the panel featured Barry Peterson, Northcreek Mezzanine; Lamar Stanley, Gen Cap America, Inc.; and John Sweeney, Baird Business Owner Solutions.

ACG CHARLOTTE, ACG MARYLAND, ACG NATIONAL CAPITAL & ACG RICHMOND

Taking on some the biggest issues of the day, four ACG chapters from the mid-Atlantic region came together to offer analysis from two leaders in finance and media. Hosting the virtual panel discussion “A Pandemic, an Election and a New Cold War,” the collaborative event featured Marc Chandler, managing partner and chief market strategist for Bannockburn Global Forex, and Kathleen Hays, a reporter and anchor at Bloomberg TV. Chandler and Hays discussed the impact of COVID-19, rivalry between the U.S. and China, and what the 2020 election means for middle-market companies and investors.



2020 MIDWEST ACG CAPITAL CONNECTION

Complete with a virtual ballroom and virtual cocktails, ACG Chicago adapted the 21st Annual Midwest ACG Capital Connection in the age of coronavirus. Despite the remote nature of the chapter's signature event, the conference hosted a record number of investment banks and provided new content for business owners.

2020 ACG RALEIGH DURHAM VIRTUAL CAPITAL CONFERENCE

ACG Raleigh Durham hosted its annual Capital Conference for the first time in an online environment. The event featured virtual coffee sessions in the morning, virtual meetings for private equity and other M&A professionals, and exclusive webinars. The event's keynote speaker was Mike Birling, vice president of the Durham Bulls Baseball Club.

UPCOMING VIRTUAL EVENTS

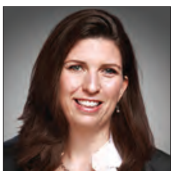
For a full list, visit acg.org/events

- **ACG Toronto** – ACG Capital Connection Virtual Conference – Nov. 2-3
- **ACG Los Angeles** – Virtual Business Conference 2020 – Nov. 4-6
- **ACG Wisconsin** – Outstanding Growth and Leadership Awards – Nov. 6
- **ACG Global** – ACG Fall Summit – Nov. 10-11
- **ACG Portland** – Fall Signature Event – Nov. 17
- **ACG Denver** – 2020 Virtual Dealmaker's Forum – Nov. 19
- **ACG New York** – Technology Conference 2020 – Dec. 14

MEMBERS ON THE MOVE

CHARLES ZALUD has joined Townsend Street Capital as vice president. Based in the firm's Birmingham, Michigan, office, Zalud plays a pivotal role in TSC's deal sourcing, due diligence and deal execution efforts. He has broad experience involving change of control acquisitions and minority equity investments in the lower middle market. Prior to joining TSC, Zalud held the role of vice president at SI Capital, a family office, where he led deal execution in the firm's direct investing mandate, covering deal sourcing, valuation, due diligence, financing arrangement and legal documentation support.

Corporate law firm Balch & Bingham announced that **LLOYD A. LIM** has joined the firm as partner, and **RACHEL THOMPSON KUBANDA** has joined as an associate. They are both part of the Creditors Rights & Bankruptcy team in the firm's Houston office. Lim brings extensive experience across a broad range of financial restructurings and bankruptcy proceedings, as well as bankruptcy-related litigation. Kubanda focuses on corporate reorganizations and restructurings, creditors' rights and trustee representation.

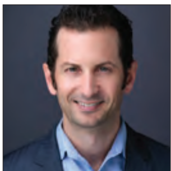


DLA LLC, a provider of internal audit, accounting and corporate advisory services, announced that **KATHLEEN LAUSTER** has joined the firm as a managing director overseeing the Capital Advisory & Restructuring practice. Lauster is based in DLA's New York metro office and leads the team in providing financial support and advising companies and creditors with strategies to unlock capital and maximize recoveries in distressed, restructuring and special situations. Prior to joining DLA, Lauster was a managing director of Restructuring & Corporate Finance at Silver Leaf Partners, LLC.

Dresner Partners, a middle-market investment bank, announced that **BRIAN V. YTTERBERG** has joined the firm as senior managing director and chief operating officer in the firm's Chicago office. He brings more than 30 years of merger and acquisition, capital raising and corporate finance transaction experience across a wide range of industries. Prior to joining Dresner Partners, Ytterberg was a managing director with XLCS Partners, a Chicago-based middle-market investment bank, where he led the execution of M&A transactions in a number of industries.

CIL Management Consultants, an international management consultancy that provides growth strategy and due diligence support to management teams and investors, announced that **AXEL LEICHUM** has joined the firm as lead partner for North America. Based in CIL's Chicago office, Leichum will focus on growing CIL's operations across the U.S., as well as providing strategic advice and working across a range of engagements for corporates and private equity firms. He joins from strategy consultancy Blue Canyon Partners.

Heartwood Partners—formerly known as Capital Partners—announced that DEMETRIOS DOUNIS has joined the firm as a managing director. Alongside other managing directors of the firm, Dounis will focus on leading new platform and add-on acquisition investments and providing oversight, guidance and support to Heartwood's portfolio of 13 companies. He will be based in the firm's Norwalk, Connecticut, office. Prior to joining Heartwood, Dounis was a partner with The Compass Group, a middle-market private equity firm, where he worked for 13 years.



CapX Partners, a provider of debt financing to small and midsize businesses, announced that MIKE WELLS (top) has joined the firm as a director. His responsibilities include Midwest business development and relationship management. Wells joins CapX from First National Capital Corporation, where he served as the firm's equipment finance originator. PAUL CLANCY (below) has also joined CapX, as a senior analyst based in Chicago. Clancy's responsibilities include direct investment underwriting, as well as helping to manage the firm's portfolio of middle-market companies and assisting with deal execution. Prior to joining CapX, Clancy was an investment banking analyst in the Technology Group at William Blair.

McCall Service, a family-owned middle-market pest control provider, announced that JENNINGS COOKSEY IV was promoted to executive vice president and general counsel, overseeing strategy and business development as well as advising the company and its board on all legal matters. He is the first member of the third generation of Cooksey family members to join McCall. Cooksey's responsibilities at the company are wide ranging and include leading the corporate development and strategy team to source and close on acquisitions, strategic partnerships and joint ventures.

Guardian Capital Partners, a middle-market private equity firm based outside of Philadelphia, announced that DAMIEN GRESKO has joined as vice president. Gresko brings to Guardian a distinct combination of deal and strategic operating experiences in public and private markets, as well as deep expertise in consumer products and manufacturing, among other industries. Most recently, Gresko led a variety of strategic initiatives to deliver growth, cost savings and capabilities for The Hershey Company.

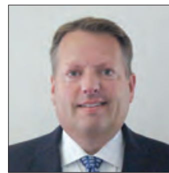
Insperity, a provider of human resources and business performance solutions based in Kingwood, Texas, announced it has promoted DANNIE DIEGO to senior strategic alliance manager. Diego has initiated and nurtured many successful partnerships that drive opportunities for Insperity's business performance advisers. She is also a leader in strategic planning, providing qualitative and quantitative analysis for programming performance for current and potential partnerships. In August, ACG endorsed Insperity as its preferred HR solution for middle-market companies. Insperity is also an Official Sponsor of Growth for ACG.

MEMBERS ON THE MOVE

UHY Advisors Inc., a provider of tax and business consulting services, announced that MATT MARTINA (top) and TODD SUTHERLAND (below) have joined the firm in its Houston office. Martina joins as managing director of International Tax Services and works with clients in Houston, as well as nationally. He has extensive experience with complex cross-border tax planning projects. Sutherland joins UHY as director of the Research and Development Tax Credit practice. He has over 20 years of experience assisting taxpayers with claiming R&D tax credits, as well as extensive experience in defending R&D tax credit claims under IRS examination.

NICK CHAMBERS has joined UHY LLP, an accounting and professional services firm, as director of the Private Equity Services Group in the firm's St. Louis office. Chambers has more than 15 years of professional accounting and industry experience working with private equity-owned companies and public registrants. He provides accounting, audit and other consulting services in a variety of industries, including manufacturing and distribution, technology, professional services, health care, life sciences, construction and energy.

The DAK Group, an investment bank headquartered in New Jersey that specializes in middle-market businesses, announced that ROBERT DEVINE has joined the firm to lead its Strategic Leadership Advisory division. Devine brings more than 35 years of experience building high-performance organizations as an executive, business owner, board member and a consultant. In his role, Devine will help guide DAK's middle-market business owner clients to refocus and adapt their companies in order to meet the changing environment.



Boutique investment bank TrueNorth Capital Partners LLC announced that MARK CROUCH has joined the firm as managing director. Crouch expands TrueNorth's presence in the Midwest with an office in Kansas City and will focus his efforts on origination and execution of both traditional and distressed M&A advisory engagements, as well as financings, joint ventures and other business arrangements. Prior to joining TrueNorth, Crouch served most recently as chief financial officer of a startup cleantech business in Kansas City. Before serving as a CFO, he spent approximately 15 years working in M&A, restructuring and leveraged finance in New York.

MORE CAREER INFO

Watch for more career information in ACG's *JobSource* monthly e-newsletter.

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IT'S THE SMALL THINGS

TRENDS IN MANUFACTURING // Work smarter, not harder

1

Rent a Robot

Just as software-as-a-service changed the software industry, companies of all sizes could soon benefit from automation by hiring robots to complete orders. Known as automation-as-a-service, this technology enables manufacturers to minimize cost and risk by renting time at factories run without human intervention. Lower capital expenditures could also reduce the barrier for new and small companies to leverage automation. The market size for automation-as-a-service is expected to reach $14.1 billion by 2025, growing at an annual rate of 27.4%. – Kenneth Research

2

Shifting to Services

As manufacturers face the challenges of shorter product lifespans, rapidly changing consumer needs, globalization and intellectual property theft, they may be forced to shift emphasis from selling products to delivering services – known as servitization. One example is Rolls-Royce, which changed its business model from making jet engines to servicing them. Experts say the practice can provide a larger and more stable source of income. – Implement Consulting Group

3

The Dangers of Deglobalization

The U.S.-China trade war and the coronavirus revealed vulnerabilities in the international supply chain, causing many companies to reorganize or pull back from foreign suppliers altogether – a process known as deglobalization. However, economists warn that deglobalization could lead to a negative feedback loop where companies and countries divest from international activity, which could lower economic growth and prompt more divestment. – TD Economics

4

Veterans Fall in to Fill Talent Gap

Manufacturers will need to fill an estimated 4.6 million manufacturing jobs by 2028, according to a report from the Manufacturing Institute. Meanwhile, more than 200,000 men and women transition out of the military each year. The opportunity is not lost on large companies like Samsung, which partnered with the Manufacturing Institute to help veterans find careers in manufacturing through its Heroes Make America initiative. – National Association of Manufacturers

5

Cyborgs on the Factory Floor

The concept of connecting human brains to machines has gained publicity due to interest from industry innovators like Elon Musk, but implications loom large for manufacturers. A brain-to-computer interface will allow humans and machines to join forces to help manufacturers make better-designed, better-produced goods. – *Industry Week*

6

A-Plus Factory Takes Shape

As concerns about sustainability and the environment mount, a number of firms are attempting to reduce the impact of their operations with factories and offices using clever design, unconventional materials and renewable sources of energy. In July, Norwegian furniture manufacturer Vestre unveiled plans for a new factory that will run on 100% renewable energy and function as a 300-acre park. Experts say the building could serve as a model for sustainable manufacturing. – *CNBC*

– Benjamin Glick

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