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Private Equity Funds as Drivers of Digitalization in Medium-sized Enterprises in Europe

Covid-19 has clarified one thing: the use of digital technologies is no longer only an option for companies – digital tools and business models have become key elements in the viability and sustainability of firms in the future. Business models and shopping patterns of customers are changing fast, and companies frequently are unable to keep pace with this change and to initiate the correct digital change processes for their long-term survival.

Experience with Covid-19 has turned a stronger technological orientation and digital normality into “a new reality“, leading world-wide to a kind of “forced digitalization“ across industries and markets. This trend is not new. It was merely intensified by the global pandemic. There has been a drastic change in consumption and shopping habits: According to a study by *Facebook*, eighty percent of customers now prefer online-shopping with shipping to the home and consider this option a faster, cheaper and more comfortable alternative to “traditional shopping“. Forty percent of customers are ready to change to new brands if their “old favorites“ are not available online. Fifty percent of customers (and this applies to B2B as well as B2C customers) are planning to retain their changed habits vis-à-vis digital business models and to accept them as integral part of the “new reality“.

This development is of great importance to business, as it points to sustained “tectonic shifts“. It underlines the importance of the course of the digital transformation and the redesign of business models towards “digital first“, also – and maybe especially – for traditional family firms.

It would be grossly negligent to ignore an increasing digital adaption and the use of information technology and data-based strategies. According to a recent

analysis of the Swiss bank *UBS*, one-digit medium-term growth is expected for production and process automation. In contrast, the *UBS* forecast is for twelve percent annual growth for the field of robotics, seven percent for industrial software and even two-digit growth for the “new markets”. According to the same study, internet penetration will reach about 85 percent of the world population by 2030, consumers will spend 70 percent of their media time digitally, e-commerce will grow by 15 percent annually over the coming ten years, *Fintech* will show an annual growth rate of 10.5 percent between 2018 and 2030 and the volume of data in the “digital universe” will increase tenfold by 2030.

This “new reality” is arriving at a time, in which a second, publicly less visible “tectonic shift” is taking place: the global, inter-generational succession of owners of family businesses. According to *Forbes*, during the coming twenty years the global economy will experience the largest transfer of wealth and property that has ever occurred. Coping with the “new reality”, while at the same time managing the generational succession at ownership and board levels, will become a decisive challenge for the long-term survival and success of family-controlled firms. If managed well, the generational change will offer immense opportunities. If missed, it will be at an enormous risk – probably the greatest single external risk facing family firms and their operational assets today. Family-owned firms, which are well prepared for succession and digitalization at the management and board levels, will wisely use the inflow of stimulus capital and allocate it to promising digital initiatives. In contrast, those who lack digital competency, will make bad investments and misallocate family capital and miss out on the opportunities offered by the “new reality” and will become victims of it.

Digital competence of the stewardship will make all the difference

In view of these tectonic shifts, modern and digitally competent stewardship will make the difference. It is typically the board that represents the long-term ownership perspective. To safeguard the survival of the firm, the digital transformation process must be started today and its consistent implementation must be ensured. For the digital transformation to be successful in the long run, owners, managers and boards, above all, must function as pioneers and must

be – or become – true digital experts. In most cases, supervisory boards of family firms lack expertise in this area. This is confirmed by recent analyses:

“Only 16 percent of all board members of the 150 biggest family firms have proven digital expertise.”¹

84 percent of all board members of the 150 biggest family firms in Germany have no digital expertise at all. For this finding, 975 curricula vitae of board members were analyzed (2021) according to three criteria:

- **Management or board experience in the digital transformation** of a comparable company (hypothesis: The person who codesigns the digital transformation of a comparable company has a profound understanding for the required change processes).
- **Entrepreneurship** (hypothesis: the person also has practical experience as an entrepreneur and brings to bear the entrepreneurial spirit).
- **Digital experience and data-based customer orientation** (hypothesis: The person has a basic technical understanding as well as profound expertise in the use of information and communication technologies. In addition, knowledge concerning digital trends, change in customer shopping patterns and its effect on value chains).

This leads to the central question: Who is to initiate and control the necessary transformation of the business model?

Private Equity Funds as drivers of digitalization in German medium-sized enterprises (*Mittelstand*)

Based on the experience of more than 700 realized digital projects of financial investors in the past ten years, the *OMMAX* team learned in numerous cases that

¹ Handelsblatt / *OMMAX*: „Partner für den Mittelstand“, 27 May 2021

digitalization is one of the core value drivers for the equity story of companies. Private Equity Funds realized this need early on, and meanwhile there are highly specialized funds in Europe that focus on the digitalization, i.e., on the digital value enhancement of companies. For the in the past five years, we found strong optimism in corresponding investors, which is reflected in higher business valuations in acquisitions, as well as in an active participation in further developing the business model during the holding period.

PE funds are meanwhile also asking for a digital due diligence within the regular due diligence, in order to evaluate the related value-added potential at the start of the investment cycle.

Based on their cross-industry experience, Private Equity Funds have recognized faster than other businesses the value-added potential of digitalization and the risks of not investing consistently and quickly in digital value-added programs. We at OMMAX always present the digital aspect very clearly in our M&A transactions, and it is a core component of the commercial due diligence. Some Private Equity Funds set up their own digital teams to implement the value-added programs in the portfolio with us. In this dynamic environment the investors digitalize their dedicated DNA and pass this on to their portfolio companies. In this way, investors are becoming pioneers who can impart a decisive impetus to the tradition-based *Mittelstand*.

**Limiting factors:
Investors are showing a high inclination to invest in digitalization – limiting factors are not money, but the speed and development of digital talent in the organization.**

How to approach digital processes in businesses?

Whenever we are not active within an M&A transaction, we start with a digital maturity analysis, focused on the company, the market and the competitors. On

this basis we develop a digital value-added program including business case and milestones, and start immediate implementation. Digital competition does not permit losing time.

The implementation focuses on the various areas of the company and is based on proven digitalization concepts (like digitalization of value added, products, distribution channels, data use and analysis, processes, as well as the development of a digital organization). Based on our self-developed database with more than 100 million data points from transactions and implementation advice, we can take data-based decisions and determine exactly the maturity and development potential of a business. In this our thinking is not short-term, but in investment cycles and holding periods.

Since we do not advise our clients only in strategic terms, but also support the implementation of the programs “from a single source“ together with our internal expert teams, we can quickly react to new trends and adapt the strategies. Our approach: Not building castles in the air, but developing reliable, sustainable and implementable solutions that can show initial success within three to six months. Meanwhile we are supporting some clients in the third ownership generation, with all *OMMAX* teams impacting significantly in the success stories, whether in the areas of transaction advisory, digital strategy or digital execution.

Investment approach *HANIEL*: Value creation for generations

■ 1. The family business

As a family business, *Haniel* has more than 260 years of experience with transformation. In the past, *Haniel* has courageously adapted its portfolio and its structures time and again to changed conditions and still has remained a family enterprise with a long tradition that has had its headquarters in Duisburg since its establishment in 1756.

The company is family-owned at 100 percent, had more than 20,400 employees in 2020 and generated sales of 3.1 billion Euro. At present, *Haniel's* portfolio

encompasses six company divisions, each of which is responsible for its own operative business. *Haniel* clearly separates management and capital: For the past 20 years, its around 750 shareholders have transferred the management to an external body.

All investments may be assigned to the segments of people, planet and progress, oriented on the UN's Sustainable Development Goals. Based on these prerequisites, *Haniel* has continuously developed its portfolio.

■ 2. DIGITAL BOARD for a successful digital transformation

For the German *Mittelstand* as well as family-owned enterprises all over Europe it is essential to embark on the digital transformation journey – especially in the “new reality” caused by Covid-19. This requires building bridges between *Mittelstand* engineering skills and innovation power on the one hand and the digitalization potential of European tech talents on the other. Professional investors as well as Private Equity Funds have installed supervisory bodies toward this end, also called “digital boards”, that help to bring digital expertise to the companies. This is well exemplified by *Haniel's* portfolio firm *CWS*, whose digital transformation will be described below.

■ 3. How HANIEL takes its portfolio firm CWS into the digital future

CWS, part of the *Haniel* portfolio, with more than 10,000 employees and sales of more than 1.18 billion Euro in 2019, is in the process of laying the foundation of a corresponding growth strategy, in collaboration with *OMMAX*. And *CWS* does not build this foundation on the classical approach focused on cost control as a means to drive earnings.

When cost control dominates the company's agenda, it takes the air out of any fundamental growth plan. *CWS* realized that there is a need to have a clear agenda for organic growth and for pursuing it systematically by building a digital future. *OMMAX* supports *CWS* in shaping this digital future. Continuous integration of a “digital board” makes *CWS* an inspiring case of how to approach the challenges as well as the opportunities of digitalization in a consistent and sustained way.

For most companies, digital transformation is an entirely new game, for *CWS*, too. With the emergence of new marketing and distribution technologies, and platforms, business intelligence and progressive analytics, digitalization has changed growth by accelerating the pace at which companies may be optimized. It is almost as if the DNA of a company is updated – although in multiple dimensions. The biggest challenge: During transformation the business must keep going.

What has to be mentioned: *CWS* is a multi-solution, multi-product and multi-segment company. “Multi” probably being the most demanding word in each company: several ESP systems, country-specific product and service catalogues, solution areas, marketing and sales to multiple persona types via multiple-stage decision steps. At this stage, a digital go-to-market strategy must contain a strong plan.

In view of this challenge, the agenda for digital transformation must be divided into manageable projects and sub-projects, workstreams and diagrams, systems and software as well as people. In the following, the agenda for the digital transformation will be presented.

■ 4. Design of the digital transformation

„The digital transformation will be successful if companies integrate their business-technology strategies from the start.“

„It is imperative to get the right partner on board, who understands the DNA of a company and effectively adds constant value along the transformation roadmap at multiple levels.“²

a) Omni-Channel

This is mostly about customer data, sales process and account management. Sounds easy? It is not. How can *CWS* optimize the sales funnel by re-shaping the sales organization and re-designing the new generation sales process as part of the new operating model?

² Adriana M. Nuneva, Chief Digital Officer *CWS*

OMMAX data scientists are helping CWS to cleanse, enrich and restructure their entire customer data across 16 markets: In the status quo setup, customer data were of limited quality and sub-optimal structure due to the obsolete system infrastructure including various ERPs and the salesforce CRM. To develop the CRM into a more effective and efficient sales tool, OMMAX developed a custom solution to optimally clean and transform the historic CRM data into a new greenfield salesforce structure.

As a result, CWS is able to accelerate its sales cycle with better CRM tactics, strengthen its cross- and up-selling opportunities between solution areas and drive efficiency in marketing and sales activities – all contributing to higher customer lifetime value across the entire customer base.

b) Content-Hub

This is all about CWS offers of products, services and solutions. OMMAX supports CWS in connecting the content hub to multiple upstream ERP systems and makes different data models manageable by unifying these into one common data set and additional solution area-specific and customer-relevant attributes. All media and unstructured marketing contents are now connected to products, services and solutions. Various downstream marketing systems can be provisioned from one single source.

c) Platforms and websites

Actually, just one website and that is new! One “global” framework containing building blocks able to design, build and deploy pages faster and in a more reliable way. This is highly relevant to running a new generation digital marketing and sales game of segment-, target-, persona-, journey-specific landing pages. Digital customer loyalty strategies with a multitude of different target groups and buying journeys create unique customer experiences from early to later stages of the sales funnel, all enabled and supported by technology and best-in-class sales tools.

d) Campaigns and marketing automation

Through tracking, grading and scoring the analysis of visitor behavior is far above simple web analytics. Marketing automation allows marketing teams to create

and manage 1-to-1 cross-channel journeys and communication with leads, prospects and customers that lead to a unified experience for the customer. Turning a broad base of unqualified leads into prospective new customers is essential. It quickly improves the efficiency of a sales funnel. Targeting and campaigns optimization funnel development and by focusing on the right opportunities at the right time. Industry best practices show an increase of 30-50 percent of the lead to sales ratio if this sales funnel step is managed well.

e) Lead generation

The crucial part of the sales process is lead generation. This is about visibility, presence and relevancy in digital channels and platforms. Profound understanding of online market dynamics, key drivers, competitive environment, and customer journey is relevant to develop a full digital roadmap and comprehensive roll-out plan. *OMMAX* supported *CWS* in implementing and rolling-out related digital initiatives, such as increasing awareness and visibility in *Google* and social media networks. The approach quickly uses the existing growth potential, increases digital reach and maximizes lead generation. Continuous optimization of digital initiatives allows steady lead generation and a growth strategy that is both agile and resilient.

f) Data analytics and business intelligence

A major part of the *CWS* digital transformation initiative is about data. *OMMAX* provides support with a holistic business intelligence approach along the entire data value chain, from data tracking and engineering, over analytics and visualization to data science. Several internal systems are connected and function as data sources to permit data-driven decision making, strategy definition and operational optimization.

g) Content creation, translation and optimization

Content is key. The right content for the right audience and in the right channel at the right time is crucial. *CWS* invests in contents that raise the profitable traffic. That is not just relevant for one country but all regions: translation and country-specific optimization are therefore key to content of lasting value. And, content is not a one-way-ticket. It needs to be curated for campaigns, landing pages, channels, audiences.

A to-do list for the digitalization process

The *OMMAX* framework provides executives, who manage such complex transformation projects, with re-platforming a complex solution landscape of competing priorities and pressures, a way to assess approaches to growth and identify the capabilities needed to follow through. While most digital transformation projects single out one primary dimension for growth, *CWS* manages a multitude of activities across different dimensions to accelerate the transition journey.

As companies consider driving their growth strategies efficiently, they need to be clear about building the capabilities (competent and, if possible, experienced internal and external teams) and practices that will help them move with greater speed and precision. Here a 3-step framework can help:

■ **1. Planning:**

Define where the value of the business lies and design the digital roadmap for the next three years.

■ **2. Developing:**

Conceptualize pilot projects and create MVPs.

■ **3. Implementing:**

Transforming and capturing the potential digital value.

Summary

Private Equity Funds are driving digitalization – especially in the *Mittelstand*. In this endeavor their financial input is important; more important, however, is an intrinsically motivated digital DNA at the corresponding PE. Digitalization, accelerated by Covid-19, and the tectonic shifts within family-owned firms by global, inter-generational succession plans, sets the priority of safeguarding over time the competitiveness of companies by way of digital transformation processes.

In 2021, only 16 percent of all board members of the 150 family-controlled German enterprises had proven digital expertise. That is why they need external partners,

but also shareholders, who can offer such expertise or at least are open-minded about it. Digital boards, like those described in the example of *Haniel/CWS*, are an effective instrument for realizing the long-term challenges and opportunities of digital change.

The ever faster turning digital wheel makes two aspects indispensable: Speed, as digital competition does not permit any hesitation, and sustained commitment. Progressing digitalization is not a short-lived trend, but will have to be on the agenda of every company in various manifestations and variations in the long term. Neglecting today to digitalize the company's DNA and either ignoring the digital transformation or failing to understand it as an intrinsic structural question, will mean not having any prospects in the future.

Many Private Equity Funds have realized this and have digital valuations ever more frequently included as an important factor in due diligence reports. The questions raised are mostly about the data infrastructure, technical scaling potentials, digital lead and customer acquisition with attractive CACs and ROI as well as digital organization. If they recognize gaps and still decide to invest, they usually push a digital roadmap after acquisition. Due to their often digitally characterized mindset, cross-industry experience and expertise, willingness to invest in digital infrastructure, they have become important drivers of digitalization.

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About the author:

DR. STEFAN SAMBOL supports medium-sized companies as well as international financial investors. As a specialist in digital M&A, strategy and implementation, he advises companies strategically and operatively on digital value generation programs focused on organic growth strategies. In addition, he supports financial investors in their acquisition and evaluation of digital business models and the assessment of value potentials. He is a known expert in the area of digital

business models and growth potentials in Europe and a popular speaker at digital conferences. Previously he was at Rocket Internet, where he promoted the development of new digital companies. He also spent six years at the consulting firm of HOMBURG & PARTNER.

He studied Business Administration at the University of Mannheim, has a Master of Science degree in Economics from the LMU Munich and holds a doctorate from the University of Bayreuth.