

7 Key Value Drivers for Generating Alpha in Private Equity Across Market Cycles

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Key Takeaways:

- Private equity (PE) firms face significant challenges in generating consistent Alpha across different market cycles. Shifting market conditions, operational inefficiencies, poor capital structures, and mistimed exits can undermine value creation and reduce returns.
- To address these issues, PE firms can focus on seven key value drivers: operational efficiency, strategic acquisitions to unlock synergies, capital structure optimisation, revenue growth, well-timed exits, sector expertise, and ESG integration. These drivers help firms navigate varying market conditions and sustain value creation.
- Implementing these strategies requires optimising operations, pursuing M&A for faster scaling, balancing leverage with risk management, driving revenue through innovation, timing exits strategically, leveraging deep sector knowledge, and embedding ESG principles to ensure long-term sustainability.

At the Private Equity Insights conference in London on 4th September, our team led a panel discussion on the key drivers for generating Alpha in private equity (PE) across different market cycles.

Joined by experts like Freya Macken from Aurelius Group, Tommy O'Sullivan from Beach Equity, Lou Gueroeva from Zanders, and John C.R. Nery from Squirle Capital, we explored strategies that help PE firms consistently outperform the market.

The ability to generate Alpha—excess returns over the market benchmark—requires a well-rounded approach. Firms must adapt their strategies based on shifting market conditions, and by leveraging the following seven value drivers, PE firms can deliver substantial returns across economic cycles.

1. Operational Efficiency: The Foundation of Value Creation

Operational efficiency is a critical lever for generating Alpha, with PE firms taking active roles in optimising the operations of their portfolio companies. This includes streamlining processes, improving supply chains, and cutting unnecessary costs, particularly in challenging economic conditions.

During the 2008 financial crisis, many firms shifted their focus towards operational restructuring, eliminating inefficiencies to preserve value and position companies for long-term growth. Similarly, Lou Gueroeva from Zanders emphasised the importance of mature treasury processes in maintaining



operational stability. She shared an example of working with Portico BOLT (a competitor to Uber), where enhancing clarity in the cash cycle from both internal and customer perspectives improved liquidity and operational efficiency.

These strategies ensure that portfolio companies run efficiently in any market condition, maximising productivity and cost savings.

2. Strategic Acquisitions: Scaling for Synergies

Mergers and acquisitions (M&A) are key to rapidly scaling PE portfolios. Acquisitions allow firms to create value by achieving synergies that organic growth may not offer, especially in bullish markets where high-growth companies are sought after to expand operations.

Tommy O’Sullivan from Beach Equity illustrated the benefits of integrating four similar organisations into a cohesive unit. This rapid integration allowed his firm to leverage the strengths of each organisation and deliver substantial value in a matter of months. Similarly, post-dot-com bubble, PE firms were able to acquire technology companies at discounted prices and realise significant returns once the market rebounded.

In both growing and distressed markets, M&A activity offers opportunities for PE firms to capitalise on growth, generate synergies, and create long-term value.

3. Leverage and Capital Structure Optimisation: Balancing Risk and Reward

Leverage is a hallmark of private equity, particularly in leveraged buyouts (LBOs), where firms use borrowed capital to finance acquisitions and amplify returns. However, leverage is a double-edged sword—it can drive high returns in strong markets but also increase risks during economic downturns.

John C.R. Nery from Squiracle Capital shared an innovative example of capital structure optimisation in the superyacht industry. By investing in a system that allowed flexible movement of ships in dry docks—comparable to playing Tetris—they could increase operational flexibility, ensuring ships could be moved out of dry dock even when others were in the way. This approach enhanced asset utilisation and operational efficiency.

Effectively balancing risk and reward through capital structure optimisation is critical for weathering market fluctuations and ensuring strong returns.

4. Revenue Growth: Expanding the Top Line

Driving top-line revenue growth is another essential driver of Alpha. PE firms deploy various strategies to expand revenues, such as launching new products, expanding into new markets, and enhancing the sales and marketing functions of their portfolio companies.



A notable example during the COVID-19 pandemic was the shift towards e-commerce, which allowed many companies to maintain growth despite widespread disruptions. Firms that invested in digital transformation were able to capitalise on emerging opportunities and drive revenue growth even in difficult environments.

These strategies allow firms to focus on growth and innovation, reinforcing core strengths to capture market share and scale rapidly.

5. Exit Timing and Strategy: Maximising Returns at the Right Moment

Timing is crucial when exiting an investment and knowing when to sell is key to maximising returns. In strong markets, firms can achieve high multiples through strategic sales or initial public offerings (IPOs). In weaker markets, careful planning is required to avoid selling at a discount.

After the 2008 financial crisis, many firms delayed exits until market conditions improved, resulting in higher valuations. Freya Macken from Aurelius Group further highlighted the importance of addressing red flags early within an organisation to boost value and ensure a more successful exit. By proactively managing these challenges, firms can optimise exit strategies and achieve higher returns.

Successful exits depend on timing, flexibility, and having a clear strategy to navigate market cycles.

6. Sector Focus and Expertise: Building Deep Industry Knowledge

Sector specialisation offers PE firms a competitive advantage, allowing them to develop deep expertise and build strong networks. This enables firms to anticipate market trends, make informed investment decisions, and strengthen operational capabilities within their portfolio companies.

For example, PE firms focused on sectors such as healthcare or technology are better positioned to identify companies with long-term growth potential. In volatile markets, this level of expertise becomes even more valuable, helping firms spot opportunities and mitigate risks.

By focusing on sector-specific strategies, PE firms can drive Alpha and enhance portfolio performance.

7. ESG Integration: Aligning Financial and Social Performance

In recent years, Environmental, Social, and Governance (ESG) considerations have become central to private equity value creation. Integrating ESG factors allows firms to manage risks better, attract socially conscious investors, and improve long-term sustainability.

Freya Macken emphasised the importance of a



strong organisational culture, which can align a company's ESG goals with broader operational objectives. Identifying red flags early and addressing them ensures that ESG considerations are embedded into management practices, driving sustainable value creation.

PE firms that prioritise ESG not only mitigate risks but also align their financial performance with wider societal goals, creating long-term value for investors and stakeholders alike.

Adapting to Market Cycles for Sustained Alpha

Generating Alpha in private equity is a multifaceted process that requires adapting to changing market conditions and focusing on key value drivers such as operational efficiency, strategic acquisitions, capital structure optimisation, and sector expertise. By mastering these seven value drivers, PE firms can continue to deliver superior returns across market cycles.

The ability to adapt and maintain a disciplined approach is what allows private equity firms to consistently outperform the market, ensuring long-term success for both firms and investors.

Meet the Experts



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