EXECUTIVE PERSPECTIVES ON TOP RISKS

Private equity-owned companies weigh impact of pandemic risks, economic conditions, labor issues and more on growth plans

When it comes to issues with that are threatening growth plans in 2022 and beyond, government policies designed to curb COVID-19, operational resilience, succession challenges, labor costs and inflation are identified as the top risk issues that companies owned by private equity (PE) worry about the most. These insights were obtained by Protiviti and NC State University's ERM Initiative in their latest survey of top risks on the minds of global boards of directors and executives in 2022 and over the next 10 years. With unanticipated events unfolding at a record pace, organizations of all types and sizes are facing massive challenges identifying the best next steps. The current landscape calls for C-suite executives and boards at PE-owned companies in particular to be vigilant in preparing for emerging issues.

While last year was a banner year for PE dealmaking, many PE firms have struggled to see desired returns on some portfolio companies, especially those in sectors adversely affected by the pandemic. Given the compressed time horizons under which many operate, PE-owned companies are under even greater pressure during this challenging period to increase efficiency, reduce cost and continue to innovate.

The pressure is evident in the high-risk ratings (6.0 or greater, which equate to a "significant" risk impact level) respondents from PE-owned companies ascribed to many of the top risk issues, compared to directors and executives in non-PE companies that participated in the survey. According to the results, leaders in PE-owned companies rated nearly half of all risk issues at the significant level; that contrasts markedly with the global results, in which no risk issue — even those in the top five — rated at the highest risk level.

Risk Category	Top 10 2022 Risk Issues	Rating
Macroeconomic	**1.** Pandemic-related government policies and regulation impact business performance	6.37
Strategic	**2.** Unprepared to manage an unexpected crisis significantly impacting our reputation	6.20
Operational	**3.** Succession challenges: ability to attract and retain top talent	6.20
Macroeconomic	**4.** Anticipated increases in labor costs may affect our opportunity to meet profitability targets	6.16
Macroeconomic	**5.** Economic conditions, including inflationary pressures, constrain growth opportunities	6.13
Macroeconomic	**6.** Adoption of digital technologies requires new skills or significant efforts to upskill/reskill existing employee	6.13
Operational	**7.** Greater expectations for our workforce to "work remotely" or for a transformed, collaborative physical work environment	6.12
Strategic	**8.** Pandemic-related market conditions reduce customer demand	6.10
Operational	**9.** Inability to utilize data analytics and "big data" to achieve market intelligence and increase productivity and efficiency	6.07
Operational	**10.** Organization's culture does not sufficiently encourage timely identification and escalation of risk issues	6.06

Key Takeaways on Risk Outlook for 2022

Respondents in PE-owned companies were well represented in this year's survey, comprising roughly one-third of the total survey respondent population. As indicated in the top 10 risk table, respondents from PE-owned companies rated the impact of pandemic-related government policies on business performance, labor costs, inflationary pressure and other economic obstructions, and talent-management issues that impede the adoption of digital technologies as top risk concerns for 2022.

The talent pipeline also is cited as an issue of central importance to PE-owned organizations. Attracting and retaining talent in today's tight labor market is a significant and persistent issue in many industries, but the nature of this risk differs slightly but notably in PE-owned organizations, where C-level leaders typically operate under constant and intense scrutiny from their PE owners. The pressure on PE-owned company leaders increases the need for executives and managers below the C-suite to not only be able to assume higher responsibilities but also have the right people in the right roles. These findings suggest that more attention should be paid to grooming the next generation of C-suite and VP-level leaders in PE-owned organizations.

Although their top risk concerns largely mirror the global results, leaders in PE-owned organizations appear significantly more concerned about the company's ability to muster sufficient resilience and agility in response to unexpected crises with the potential to inflict reputational damage. Of note, CFO respondents (in both PE-owned and non-PE-owned companies) placed a similar emphasis on resilience and agility, also rating it as a more significant concern than all executives and directors did. The resilience concern underscores the need for PE-owned company leaders to continue to contemplate resilience events that fall outside their preconceived notions of what is possible. In this high-risk landscape, the ability to reimagine events that can happen rapidly, without warning, and may occur in concert with other crippling and uncorrelated incidents is critical.

Overview of Top Risks for PE-Owned Companies in 2031

When looking ahead a decade, the top risks that leaders in PE-owned organizations identify include fending off competitive challenges from new marketplace entrants, navigating economic conditions that restrict growth opportunities (and squeeze margins), and competing for increasingly valuable digital skills. Talent management concerns also figure prominently among the top risks for 2031. PE-owned organizations' sharp focus on shorter time horizons is also apparent in the comparatively lower risk ratings these respondents assign to issues for 2031.

Of course, some risks never fade away; certain issues require sustained vigilance today and over the long haul. This is certainly the case when it comes to the ease with which future new competitors, along with other major changes in the competitive environment (e.g., major market concentrations due to M&A activity), could threaten the PE-owned organization's market share.

Leaders within PE-owned companies also expect talent-management challenges and skills shortages related to the voracious adoption of digital technologies and advanced tools (such as artificial intelligence and machine learning today as well as quantum computing in the months and years to come) to sustain as a top risk in the coming decade. This challenge has more than one dimension in PE-owned companies, whose finance and accounting, compliance, and internal audit functions frequently have a pressing need to install new automation and digital tools (and related skills) as they ramp up for IPOs and the regulatory scrutiny that follows.

Risk Category	Top 10 2031 Risk Issues	Rating
Macroeconomic	**1.** Ease of entrance of new competitors and other industry changes threaten market share	6.07
Macroeconomic	**2.** Economic conditions, including inflationary pressures, constrain growth opportunities	5.91
Macroeconomic	**3.** Adoption of digital technologies requires new skills or significant efforts to upskill/reskill existing employee	5.86
Operational	**4.** Succession challenges: ability to attract and retain top talent	5.80
Strategic	**5.** Substitute products and services arise that affect the viability of our business	5.76
Operational	**6.** Resistance to change culture, operations and the business model	5.76
Strategic	**7.** Rapid speed of disruptive innovation outpaces our ability to compete	5.76
Macroeconomic	**8.** Ability to access sufficient capital/liquidity	5.75
Operational	**9.** Hybrid work environment and changes in nature of work challenge ability to compete	5.74
Operational	**10.** Uncertainty surrounding the viability of key suppliers, scarcity of supply, or stable supply prices	5.68

In Closing

Leaders in PE-owned organizations rate far more risk issues as significant concerns today. While these leaders tend to confront more short-term performance pressure compared to their peers at non-PE-owned companies, they also know that few, if any, of their top risk concerns will go away anytime soon. Thriving in the face of current pressures will help lessen the impacts of future risks.

"The last few years have highlighted the need for private equity leaders to evolve their internal and portfolio company organizational models and build new capabilities quickly and concurrently to drive value. To be successful, they must focus on innovative and intensive due diligence, broad implementation of operational resilience practices, and manage multiple priorities and risks at the same time to keep pace with the transformational changes in today's environment."

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