KEYNOTE INTERVIEW

PE's AI playbook



Private equity's interventionist approach is accelerating AI adoption across portfolio companies, as GPs also explore applications in their own operations, say Bridget Walsh, Kenneth Woodruff and Prashant Garg at EY

Q To what extent are private equity firms embracing AI and where are they looking to deploy it?

Bridget Walsh: While our private equity clients are at different stages in the AI adoption journey, given their interventionist nature, we see them leading the way.

At the fund level, firms are using AI to improve operational effectiveness and efficiency – uncovering new investment opportunities, streamlining the dealmaking process and enhancing the flow of critical information between LPs and GPs. According to EY research, 84 percent of funds predict AI will have a significant to transformational impact on their business, so they clearly see the potential.

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These firms are leveraging AI in deal sourcing, considering the $1.4 trillion of dry powder awaiting deployment. Our tools can quickly identify businesses that align with specific criteria within particular sectors, thereby facilitating origination.

When it comes to deals, the most frequent question we get asked is how AI is likely to disrupt specific sectors or business models. Will it render them obsolete, or will it turbocharge the business case? Thinking about the opportunities and risks ahead can be a valuable differentiator in a competitive bidding environment.

AI can also help private equity firms store, mine and interrogate vast amounts of data, collated by them over many years, in a more effective way. This data can typically comprise information from hundreds of businesses they have managed through different sector-based cycles and macroeconomic backdrops. We have AI tools capable of mining this data, delivering insights to support the investment decision-making process.

However, arguably the most powerful transformation is occurring within the portfolio, where AI can challenge existing business models and supercharge value creation.

In fact, firms are increasingly incorporating AI strategies into their 100-day plans. EY teams are working with clients to use generative AI to grow revenue, reduce costs and improve productivity. For example, we help them deliver innovative customer support with generative AI to drive significant productivity savings.

Overall, we are seeing a great appetite and momentum within PE to adopt AI into their operations and across the investment lifecycle and the results are impactful.

Q How are firms thinking about scaling the use of AI across their portfolios and why is this important?

Kenneth Woodruff: Private equity firms currently have around 28,000 companies sitting in their portfolios, all of which they are looking to monetise. Holding periods have extended significantly over the past two years and LPs are increasingly demanding liquidity as a result.

The onus is therefore on GPs to transform their portfolio companies by leveraging the latest technologies. That could mean the difference between a successful and a suboptimal exit as buyers and sellers finally come together on valuations and deal activity starts moving once again. That, in turn, of course, will help propel the firm's fundraising fortunes.

But while a couple of big AI-driven wins are certainly to be welcomed, firms that can scale or repeat this success across their entire portfolio are the ones that are really going to outperform their peers, raise ever larger funds and ensure the sustainability of their business model.

There are two ways in which we are seeing private equity firms look to achieve this goal. The first is a bottom-up approach, piloting different AI schemes within an individual portfolio company and then attempting to extend that across the wider portfolio if successful. However, larger clients with the dollars to put to work are starting out with a 'tiger team' – a group of focused specialists – at the top instead. That team is conducting research and creating a playbook, before piloting solutions and rolling them out in that way.

Certainly, we are finding that an AI playbook, including detailed methodologies around how solutions are going to be developed, what technologies are going to be used and what best practices are to be advocated, can prove key to success.

It can also be helpful to bring portfolio companies together. We have seen several clients have early success with AI centres of excellence, where portfolio companies are encouraged to cross pollinate ideas. That can help drive adoption across the portfolio.

Prashant Garg: AI playbooks focusing on specific functions within an organisation, such as supply chain

Q Faced with so much potential, how can GPs and their portfolio companies decide where to prioritise AI integration?

KW: A recent survey we conducted revealed that investment in technology, including AI, to improve growth and productivity, was the top strategic priority for private equity-backed CEOs over the next 12 months. The challenge that these CEOs face, however, is identifying where and how to leverage AI to produce the best outcomes. This is particularly important because AI adoption typically requires significant upfront investment both in the AI capabilities themselves, as well as in training people and transforming processes.

Indeed, one in four CEO respondents to our survey said they have trouble distinguishing between hype and meaningful use cases. As a result of some of this frustration, our conversations with clients have become less about the art of the possible and more about an exploration of what is practical. They want to know how we have helped others and what has resulted in tangible, positive change, enhanced efficiency and value gain.

EY teams are supporting PE clients throughout their AI journey. At one portfolio company, we have leveraged AI to improve call centre agent efficiency by 15 percent, and at a global fund, reduced the time required to process credit contracts by around 75 percent.

management, operations or HR, can be particularly effective. This targeted approach allows for the integration of AI in functions. By doing so, it significantly enhances the operational efficiency and positively impacts operational costs.

Q How are the latest advances in generative AI helping build on the data analytics capabilities that many PE firms have been honing in recent years?

PG: Advanced analytics and machine learning are very good at analysing structured data and helping to make predictions about the future based on what has happened in the past. However, around 80 percent of the data that sits in any organisation is unstructured data – all the information that exists in various documents and e-mails. Generative AI offers the ability to interrogate that unstructured data at scale and in a seamless fashion, allowing firms to use that information in real time.

Q What are some of the risks associated with the use of generative AI and how can these be overcome?

KW: The worst-case scenario is bad data resulting in incorrect answers. That is why it is so important to have sources cited and linked, so it is possible to quickly verify that the information extracted has been interpreted correctly. It is vital not to blindly accept answers until users have sufficient confidence in the data and the AI process itself.

PG: I concur that it is essential to trace back to the information source, maintaining human oversight to prevent inaccuracies, biases or errors in the generated answers. Hallucinations are a significant worry for private equity investors. In our survey, 60 percent of senior private equity leaders expressed personal concerns about the responsible use of AI, a concern that has grown over time. Rather than responding to those concerns by avoiding the use of AI, however, firms are responding by building appropriate AI governance frameworks into their organisations.

"AI can challenge existing business models and supercharge value creation"

BRIDGET WALSH

"Generative AI offers the ability to interrogate unstructured data at scale and in a seamless fashion"

PRASHANT GARG

KW: The other challenge I would point to is ensuring that introducing AI doesn't slow the business down. It can be a bit like changing the engine while in flight, so you need to be pragmatic about the changes you choose to make and how those changes are integrated.

We have had discussions with several firms that have shown great interest in AI adoption but that have ultimately chosen to apply the brakes. They have recognised the importance of taking time to understand the way their deal teams operate, and the way their operating teams operate, ensuring they are not inflicting too much change in a way that could have a detrimental effect on the operations of existing companies or on deal processes. AI needs to be a force multiplier and not something that slows the business down.

Q How transformative do you believe generative AI will ultimately be for the private equity industry?

BW: One of my clients shared with me recently that they just need one portfolio company to be sold at a huge multiple because of the way generative AI has been implemented for AI adoption to really go into another gear.

However, while I do believe the AI journey is going to play out quickly, particularly in the context of private equity, as with any tech adoption, there will be firms operating at different ends of the spectrum. Our job is to help support all those firms, providing them with practical examples of value added and costs saved, rather than simply theory, and that is something we are increasingly able to do.

PG: I would emphasise that the evolution of generative AI will focus on comprehensive workflows that can revolutionise processes and functions, diminishing the need for previous levels of human intervention. This marks the trajectory of advancement in this field. ■

Bridget Walsh is the EY Global Private Equity Leader, Kenneth Woodruff is the EY Americas Private Equity Technology Leader, and Prashant Garg is a Technology Consulting Partner at Ernst & Young LLP, India.