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Blue Chip Recruits and Deal Flow

A rundown of the best practices for private equity business development professionals

By Mark Jones

The first Wednesday in February may not mean much to a majority of the population, but to rabid college football fans it is one of the two most important days of the year. In these circles, folks prefer the simple moniker of Signing Day. This is the day when Florida tries to ink another Tim Tebow and when USC hopes that the next Reggie Bush will commit to wearing cardinal and gold. Signing day is the culmination of years of legwork by coaches who have combed the countryside looking for Saturday's future superstars and spent many a Friday night in small town high school stands from Pahokee, FL to Abilene, TX.

On the private equity gridiron, a large portion of the responsibility for signing up the next triple digit IRR deal falls on the LBO road warrior, the business development officer (BDO). As PE has become an increasingly crowded field with hundreds of millions in un-invested capital, most middle market LBO shops have institutionalized the BDO position to a level where it is a critical aspect of the business model. One could certainly argue that private equity is in the "mature stage" of the four-stage product lifecycle. Brand differentiation is critical at this stage and business development is no exception.

During my fifteen years in the PE BDO arena, I have seen many different models for deal generation. Whether the function be centralized under one person in one location or spread across several professionals in a multi-office format; whether staffed by junior marketing associates or by partner level decision makers, there are numerous ways to keep the pipeline full. Whatever the model, are there any common keys to a successful business development effort? To answer that question, I solicited perspectives from a handful of PE and investment banking friends. These industry veterans had great

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insights into what works best when it comes to PE marketing (getting your firm on the deal flow radar) and sales (closing an acquisition).

When I got into this business, I certainly could have used a copy of "Deal Flow Generation for Dummies." Instead, my partners simply told me to go find some good companies to buy. That was helpful. Jim Marra, Director of Business Development at Blue Point Capital Partners, would counsel a new BDO to figure out a few things before starting to rack up the frequent flyer miles. First and foremost, determine your firm's "deal box" in terms of preferred size, industries, situations, geography and pricing metrics, as well as what quickly kills a deal in your shop. This information will more efficiently focus your efforts and save your most scarce resource—-time. You will also be able to more effectively communicate your "message" to your target audience. In a world of 1,500-plus PEGs, your message should be simple to articulate as well as consistent in presentation and application. "Style drift," in investing parlance, can be bad for biz dev, not to mention what your LPs will think. The reality is that the market will decide your "center-of-the-plate deal" and it is your responsibility to steer that decision. Without effective guidance from the BDO, an intermediary may simply choose not to present a deal to a PE shop under the assumption that it is not a fit.

Familiarity breeds comfort, so seeing more deals starts with showing up. **Bo Briggs**, a managing director at **Croft & Bender**, says that even in 2010, shoe leather matters. I have always been a big believer that nothing beats a one-on-one meeting in an investment banker's office or over a meal. If I am meeting an intermediary for the first time, what do I want to accomplish? Succinctly put, I want to convey my firm's strengths and take a first step toward building a relationship.

Dave Dunstan, a managing director at **Western Reserve Partners**, relays that everyone is smart and everyone has money, so the PEGs who try to build relationships stand out. One guiding hint is that approaching a meeting from the perspective of "tell me about you and your firm" is much better than "let me tell you about how many good deals we have done." Along those same lines, check your ego at the door. One investment banking pro bluntly told me that this industry creates too much hubris. He believes that we are all salesmen, so what's with the attitude? Remember that, to this intermediary, you ARE your firm and that every word and action is being viewed from the perspective of "do I want to introduce this PEG to one of my valuable clients?"

A fellow PEG BDO who met me for the first time gave me a first hand example of a comment that could be misconstrued as condescending. He asked where I was from and I replied "Chattanooga." With a smirk, he asked if we had an airport. I'm not sure he had a clue as to how badly that comment came across and I wondered how he interacted with intermediaries. And, just for the record, we do have an airport (although it may be closed on Wednesdays in the summer).

One issue that was consistent in my discussions with i-bankers is that they prefer dealing with someone who speaks for the firm. The BDO doesn't necessarily have to be at the partner level, although it helps, but should be able to say what deals a firm will or will not do. This means being able to ask some basic questions to determine if the deal is a total non-starter. Investment bankers grow increasingly weary of empty suit book collectors, ie., very junior people who want to see every CIM. By the way, a couple of comments on meeting manners are worth mentioning. One, don't have your secretary set up the meetings. Most i-bankers appreciate a personal email to which is attached a one page firm summary that communicates the firm's salient aspects. Two, showing up is good, but showing up or calling every two months to ask what is new can be a bit "smothering." The same advice goes for marketing email — less can be more. Finally, if something comes from the meeting that requires follow up, don't let it slip between the cracks.

Doing more than city marketing blitzes is a reality for many BDOs. This extra effort means attending a variety of industry conferences, writing articles, speaking on panels, and then some. I have attended an incalculable number of M&A/PE events where deal sources are present. I have spoken as a moderator or panelist at events hosted by ACG Chapters, Buyouts, AMAA, IBBA, CFA, FEI, TMA and even the local Chapter of the Tennessee Society of CPAs. I mention these efforts not to grandstand, as, guess what, there are a lot of other PE BDOs who do the same thing in an effort to widen the top end of deal funnel. Does this mean occasionally pushing one's comfort zone? You bet. But, over time, you get used to it and, in some twisted way, you might start to enjoy taking unscripted questions from a large crowd.

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I should mention that if you are going to speak in public, remember that your audience may not be homogeneous and could contain a variety a constituencies so be careful what you say. I saw this scenario first hand on a panel in NYC where one of my fellow panelists, the president of a very well known middle market PE group, addressed the audience as though it was comprised solely of LPs. I make this assumption as he boasted about not participating in auctions (I guess he's found the secret stash of proprietary deals) and only paying low multiples for companies. As I looked around the room and saw a number of deal sources, I had to wonder what the heck he was thinking. As to maximizing the benefits of attending conferences, which could be an article unto itself, the BDO should remember their college exams — the best grades came on the tests for which they were most prepared. In other words, do your homework to fill your days with productive meetings, schedule lunches and dinners and watch out for those late nights. Another way to stand out from the crowd is to host an annual marketing event that is truly unique. A great example can be found every winter on the frozen Minnesota waters of Lake Mille Lacs where the mezzanine firm of Northstar Capital hosts its unparalleled "ice fishing" excursion.

When an intermediary wants to introduce you to a deal, for goodness sakes be responsive. **Alex Mammen**, a managing director with **TM Capital**, asserts that investment bankers walk in the shoes of clients and lack of responsiveness can be a harbinger. This part of the process is another area where seasoning helps with knowing the handful of important provisions in a CA as well as if a given deal is consistent with the firm's strategy. And this includes add-ons as well as platforms. If an existing portfolio is not in acquisition mode, then say so. The same goes for a platform company that is in an industry where there is negative institutional memory.

Phil Curatilo, a principal with **Key Principal Partners**, relates that the market needs to be confident in your ability to screen deals. Being responsive is certainly important, but balance responsiveness with giving the deal a fare shake. For example, a turn down after quickly skimming the executive summary doesn't count. If that's all it takes, the CIM shouldn't have been requested in the first place. Once the deal passes the "sniff" test and goes into the process for serious review, the real analysis starts. This internal aspect of business development is the part of the sausage factory that most i-bankers don't see, but is so critical. Figuring out which deals to really chase is a learned art. There are good deals and then there are good deals that have a reasonable likelihood of closing.

Further, pride of authorship should be avoided such that a deal is not my deal or your deal, but our deal. Assuming the presence of a team mentality, someone in the firm still needs to be the deal's sponsor by taking ownership in it. The BDO that assumes this sponsor role can foster a level of trust with his colleagues at this point by being smart on the major issues surrounding a potential investment such that they can be intelligently discussed in a deal vetting meeting. And the BDO shouldn't be thin skinned by tough questions from colleagues. Trust me; your LPs will appreciate a healthy dose of skepticism. A recommendation to BDOs on the internal sale process: don't rush your partners to make a decision. As one of my old bosses used to say: "If the answer has to be today, then the answer is no." One piece of advice for the "internal" partners of a PE shop is that perfect deals at perfect prices are virtually mythical. As such, if you are waiting for a fast growing, high margin company with no competitors and no material weaknesses that is priced at four times Ebitda, you'll be waiting a while.

When BDOs relay a decision not to pursue a transaction, they face one of the hardest parts of the job: saying "no" in a manner that is not detrimental to the relationship. After all, "do not call lists" are a reality. Make it is obvious that you devoted enough time to arrive at your decision. Tell the deal source specifically why you are taking a pass. Furthermore, suggest other possible buyers, PEGs or strategics. I once passed on a transaction, but suggested several other PE groups as alternatives. One of those PEGs ended up being the buyer. That's a quick way to build a long-lasting relationship.

Alan Mayer, a managing director with **GMB Business Advisors**, relates that a PEG once made an executive in residence available to discuss a specific industry and help identify alternative buyers. That PEG now sees all of Alan's sell-side opportunities. Bottom line, no interaction concerning one deal should be about one deal. The focus should be on the relationship, as that deal source may present a PEG with dozens (or more) of opportunities in the coming years.

Assuming a PEG submits a compelling indication of interest (IOI), the next step is to meet company management. In the deal world, management meetings might be the closest thing we have to "show time" since a lot can go right or wrong as emphasis shifts from marketing to sales. The broad advice I would relay here is: One, be prepared. Two, be ready to sell. Three, everyone you bring to the meeting will be a reflection of you. Preparation may sound like common sense, but an i-banker confided to me that eight PEGs are often invited and four are unprepared. The wise PEG will do a lot of homework on the people and the company.

Starting with the people, **Eric Malchow**, a managing director with **Lincoln International**, recommends asking for a dinner the night before as a way to develop a social rapport before the meeting. I would add that if you ask for such a dinner, and especially if you order a bottle of Screaming Eagle Cabernet, don't get alligator arms when the check arrives. In terms of preparation, asking insightful questions is a sure way to convey your level of homework. And this goes for all of the PEG attendees. You'd be surprised at how many i-bankers told me about PE partners who obviously "outsourced" the meeting preparation to the junior professional.

Jason Payne, a managing partner with **Mainsail Partners**, relays that his goal is to not necessarily to overwhelm management with numbers of questions, but to ask the three "right" questions so as to convey that he "gets it." Meeting preparation should include asking the i-bankers for insights into any situational dynamics that might not be obvious in a CIM. Much information is relayed in these meetings, but **David Santoni**, a partner with **Prestwick Partners**, maintains that someone from the PEG better be able to sell. Especially in a case where the incumbent management will retain equity, the effective articulation of a PEG's track record and value-add can be nearly as important as monetary consideration. In all management meetings that my firm attends, we present the results of every investment we have made in our 20-plus year history. More than a few investment bankers have complimented us on this level of transparency. After all, it is transparency that can allay fears of the dreaded retrade down the road.

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A wise PEG is mindful that, in the eyes of the seller, the lenders or industry "experts" that the PEG invites to the meeting are viewed as being members of the PEG's team. Accordingly, rules of the road should be established in advance of the meeting so as to avoid any potential breeches of decorum. Most every investment banker viewed the "industry expert" concept as a risky proposition at this stage. It can be a positive in terms of industry knowledge, but can also be a huge negative if the individual comes across to management as "this is how things should be done".

Bud Applebaum, a principal at **Wingate Partners**, feels that if an industry expert or operating partner is at the initial meeting, it is crucial to get management from "what's this guy's role?" to "this guy could really help me." Above all, remember that this stage is the first step toward establishing a relationship with a management team that may only go through such a process once in their careers. As such, treat them, and the investment banker, as the most important people in the room.

Bill Glastris, a founding principal at **Prospect Partners**, strives to convey that being a boss is easy, but that Prospect knows how to be a partner. Further, when a management team looks back on an experience with Prospect, Bill wants them to remember the partnership, the respect and value-add that they brought to the table as well as the capital.

Following the management meeting, some buyers drop out and some sharpen their pencils in hopes of gaining exclusivity. Unless a buyer is offering to pay a materially higher price with no closing contingencies, the process remains competitive. Some truisms: the LOI should be consistent with the IOI, specificity is critical, as is understanding & addressing all of management's "hot buttons", contingencies should be minimized, due diligence (time spent in the data room as an example) should be maximized and enthusiasm about a deal helps, so show it. Every company has "issues" and the smart PEG conveys a knowledge of and comfort with these issues as another way to exhibit certainty of close. Don't expect to sign the LOI and then hire a third party consultant to validate the business plan — that's the kind of work that should have already been done.

The wise PEG does plenty of due diligence but also realizes that an investment banker who perceives "paralysis by analysis" is likely to go in another direction. Reinforcing this need for certainty, many entrepreneurs are growing fatigued of the process at this point so PEGs should be sensitive to this situation. Ultimately, an investment banker will advise the seller to consider two key questions: one, with whom do I want to partner for the next five or more years, and two, who is most likely to get this done?

A comment on valuation is also worth mentioning. All investment bankers agree that the buyer is most definitely not always the high bidder. Although I couldn't get a quantitative answer to the question of "how much lower is too low"?, I feel it safe to say that $40 million will probably not beat $50 million, but $46 million just might depending on the numerous other transactional issues. After all, it is the banker's goal to balance the best match of economics and chemistry since satisfied sellers are an excellent referral source.

Over the years, I have learned a few things that are applicable at a variety of points in the business development process. Everyone is a potential deal source so your professionalism should be pervasive and consistent. If an intermediary you have never heard of contacts you with a deal that is not a fit with your firm, respond with a polite email that is copied to other principals at the firm. This simple act is important as some firms centralize relationships while at others it is more specific to each banker.

Anything you can do to stand out is an attribute. For example, if your conference registration includes two attendee slots, offer the second one to a local intermediary. If a company contacts you directly for capital, refer them to a few good intermediaries. If an intermediary mentions that they are having a hard time financing a deal, offer some names of lenders who might be interested.

Relationships can take time, so keep at it. Occasionally, you won't connect with a particular deal source for some reason. That's okay. In the age of technology and social networking, don't underestimate the power of a handwritten thank you note. Let a deal source get to know your colleagues as it is another way to deepen the relationship. The firms that excel at business development often have a firm-wide sales culture and an appreciation for the competitiveness and ever-increasing level of market efficiencies. **Paul Sperry**, co-founder and president of **Sperry Mitchell**, reminded me that their clients pay them for their judgment. As such, don't give a deal source any reason to question yours.

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Finally, and this is perhaps one of the most important aspects of business development since it relates to continuous improvement, learn from your peers. It is impossible for me to articulate all that I have learned from the ladies and gents who do this job well. I'm not about to name names as I'll surely forget someone, but to all those folks with whom I have partnered on intermediary dinners, shared war stories of how many marketing calls can possibly be squeezed into one day (I think my record is ten including the early morning run with an i-banker) or commiserated about a cancelled flight, I thank you for your friendship and wisdom.

Oh yeah, I mentioned Signing Day as one of the two most important days of the year for us college football nuts. So what's the other one? Well, the first big kick off weekend this Fall is September 4th. I can't wait.

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