



MARGIE MANNING

TAMPA PRIVATE EQUITY FIRM SAYS 'YES' TO INVEST MORE

KLH Capital partners (from left): Kyle Madden, Will Dowden, Chris Hart and James Darnell

One of the largest private equity firms in Tampa Bay has changed the investment strategy for its newest fund so that it can do more deals.

KLH Capital is willing to take a minority stake in the businesses in which it invests the proceeds of KLH Capital Fund III LP, which raised \$135 million in committed capital.

"If we see people with a solid business model and they are a good management team, we hate to watch the opportunity to partner with them walk by, simply over the dogma 'I gotta own 51 percent,'" Dowden said. "We were getting asked a lot of times and historically we said no. Now we can say yes. We think it opens the funnel a little bit."

Dowden, along with two newly promoted partners at KLH, Christopher Hart and Kyle Madden, sat down with *Tampa Bay Business Journal* for a wide-ranging discussion about private equity.

Here are excerpts of the conversation, edited for brevity and clarity.

How hard was it to raise funding for the KLH Capital Fund III?

DOWDEN: Our investor base is all private capital, we don't have any institutional investors like banks or pension funds or endowments. Fortunately Fund I and Fund II were quite successful and that made the fund-raising process probably easier for us than others. We went back to the same investors in Fund I and Fund II and asked them if what they wanted to do for round three. That was a pretty short and easy conversation. After two successful funds, with the same people, it wasn't that difficult to raise. It's been up and running since April 1 and we've made our first investment already in Bonita Marie International. They are a supplier to the redemption merchandise market.

What is that?

HART: A good example might be at Chuck E. Cheese's or a Dave & Buster's; any retail establishment with in-house games or activities where you earn points or tickets that you can redeem for small goodies, plush toys, electronic goods. BMI is the distributor and inventory replenishment mechanism.

DOWDEN: BMI has very integrated inventory management system that allows their customers to run with effectively no inventory except what's on their shelves. We replenish it weekly or however often we need to. BMI also does the merchandising – the process of picking what goes on the shelves. If you are an operator of a limited number of stores, you may not have a full-time person dedicated to buying goods, stocking them, picking what goes on the shelves, etc. BMI can do that entire thing for you.

Why did you change the control strategy for Fund III?

HART: From a business development perspective, we've identified a lot of situations over the past few years where a business owner was considering both options, but it was pretty clear that they still had a lot of growth potential in the business. They had a vision for it, and they would have enjoyed realizing a lot of that value before exiting, but still wanted to have a liquidity event. We can do a control situation and they can maintain a meaningful amount of equity, but that may

not be what they prefer. This gives us another option.

MADDEN: We're still looking for the same management buyout, generational transfer or owner-operator recapitalization, but to Chris' point, it's the flexibility that we're really excited about. We've come across a lot of family dynamics, where some may want to buy out or inherit the business from dad but still want to remain in a majority control position. So it's increased flexibility across the board.

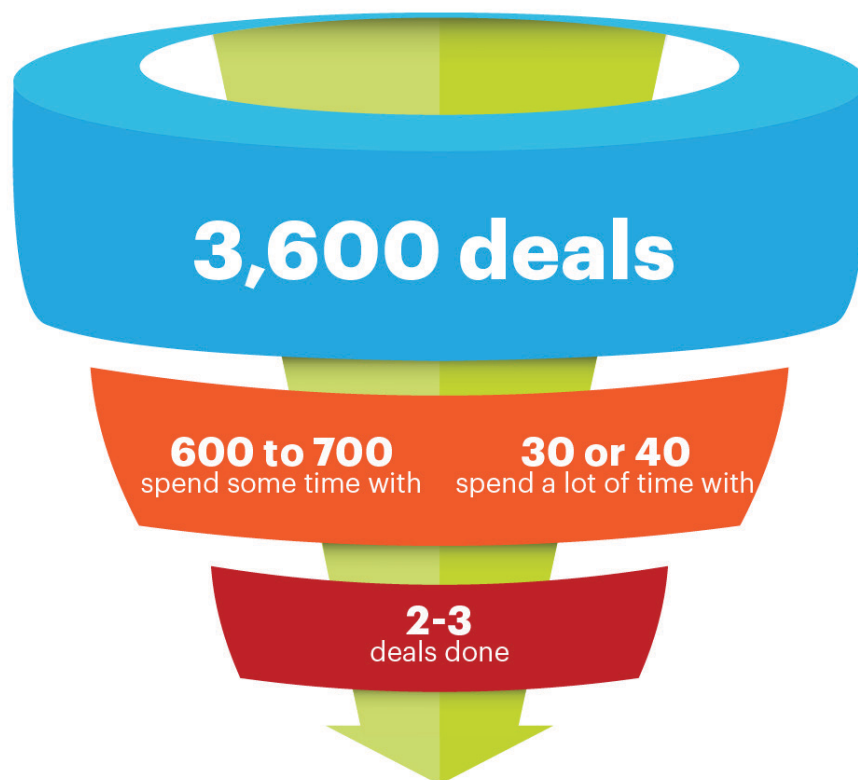
DOWDEN: We will compete more with folks who do traditional cash flow lending or mezzanine lending. Mezzanine lenders will take minority ownership positions sometimes. But we offer a different value proposition. Our partner-to-portfolio company ratio is much lower. We're at less than two companies per partner. We can spend a lot of time with the companies when they need it, when they are doing an acquisition, or recruiting a new CFO or COO, or putting in a new accounting system.

What's your assessment of private equity in the Tampa Bay area?

DOWDEN: For not being a financial hub, the level of sophistication and awareness of private equity is really high in Tampa.

HART: I also think the appreciation of private equity is well-received. Sometimes private equity gets a bad reputation, but that speaks wonders to the firms down here.

DOWDEN: There's not as many private equity firms locally investing locally. This is very much a seller's town. Anecdotally, a lot of the deals that get done around Tampa are sales to strategic buyers. I don't know why that is and I don't know why there's not more opportunity for private equity to play a role in M&A locally. I'm a little surprised by the lack of Tampa private equity investing in Bay area businesses.



KYLEE CRESS

Bonita Marie International is headquartered in New Jersey. Do you look for candidates here?

DOWDEN: Yes, we have two investments in Lakeland – Mid-State Machine and Fabricating and Uretek Holdings, which recently changed its name to Ground Works Solutions. We had an investment in TSR, in Sarasota. And we've invested in other Florida businesses. We like investing in Florida. Part of the reason that we've been less successful locally is there's a lot of tech services and health care and real estate development going on. Those are big pieces of our community and those aren't sectors we invest in. For us, it's just a tougher market. We're business services, but not the high tech stuff. It's business services, industrial services, industrial distribution.

MADDEN: Central Florida is an interesting neighborhood for us because of the types of businesses and the family situations that we're being introduced to.

How many deals do you have in your pipeline?

DOWDEN: Last year, we saw 3,600 deals, most of which are not a fit. There are 600 to 700 deals we spend some time with, 30 or 40 we spend a lot of time with, and two or three that we invest in. We'd love to do 10 to 12 deals over the next four years.

How long do you hold them?

DOWDEN: Right about five years. But we don't have to sell anything. That's the advantage of our private capital base. We can wait for the right time and don't have external pressures to exit prematurely.

Can you talk about rate of return?

MADDEN: No, but the ability to raise Fund III shows evidence we've been successful.

DOWDEN: We're absolutely top quartile.