

Favorable Odds

by Thomas Bonney

In the movies, Las Vegas provides a larger-than-life dramatic and comedic backdrop for pursuit of big dreams. From "Vegas Vacation" to "Casino" to "Swingers," scores of characters have put their own version of "everything" on the line to chase the lure of this town's enormous possibilities.

Of course, we know not everyone leaves Vegas a winner. And in light of today's market conditions, scenes like Clark Griswold's blackjack losing streak in "Vegas Vacation" may feel a bit too personal. Down to five dollars at a ten-dollar minimum table, he asks the dealer, "What can I do with five dollars?" The dealer quips, "Gee, I don't know. Buy a bullet and rent a gun?"

So as we gather in the other "City that Never Sleeps" for the 2009 ACG InterGrowth Conference, our first inclination might be to ponder private equity's current dynamics of risk and loss, but I challenge you to focus instead on our strong history and the enormous possibilities ahead.

What Middle-Market Private Equity Has Done Right

We've helped family businesses make desired transitions. Over the past 15 years, private equity has become a viable exit possibility for most family businesses, provoking discussions amongst families about transition in the face of family discontent, limitations in existing management's expertise and desires, and interest in taking financial risks to get to the next level. Many have talked about the jobs that PE cuts, but few talk about the entire enterprises that have prospered with the infusion of PE talent, capital, and focus on competitive, strategic, organic and bolt-on acquisition-oriented growth.

We've fostered enterprise-level growth. Professional ownership often brings a more comprehensive and quantifiable understanding of market size, competitive position within the market, and the steps necessary to move forward in a rational manner to enhance both market share and competitive position.

We've created reporting and control environments for positive change. Professional ownership can rapidly change the culture of a family business by enhancing visibility and driving the creation of actionable information for management's decision-making. Key Performance Indicators, rolling 13-week cash flow forecasts, and sales and margin by customer type become the new information that provides the insight and foundation to make bold moves forward.

What Will It Take to Reset Our Industry for Growth?

We need visibility. Clark Griswold had a map and visibility of the road ahead. We have neither and need to get both back quickly. CEOs and PE execs we work with every day are hesitant because they cannot see beyond the sales backlog report, and even then customers with booked sales may cancel, regardless of cancellation provisions in the contract. Our economy needs visibility, even if we don't like what we see.



Fix the credit markets, please. Our brethren at the large banks and the Treasury must return credit to pre-bubble levels. We have played around the edges because enterprises were "too big to fail." I now conclude the downside to keeping them alive is greater than the downside to liquidating and reorganizing.

There is no talent glut; there is a resume glut. We need real leadership and talent upgrades at portfolio companies; in today's challenging economic times, access to A players and the ability to recruit and retain them are critical to success. Conventional thinking indicates there is talent on the street, and we have seen more on the street now than in the past several years. However, talent remains scarce and intense focus continues to be required in this critical area.

What Promising Trends Lie on the Other Side?

Stronger portfolio holdings ready for an upswing. We estimate the decline will begin to subside in the fourth quarter of 2009. By then, we will all have spent 12 to 18 months creating lean, mean fighting machines laden with talent at our portfolios that make it through to the other side. I suspect cost advantages that many companies in the developing world had over U.S. companies will narrow and we will be in a better position vis-a-vis cost of production to compete globally.

Clearer competitive landscape. No longer will the marketplace for our goods and services be littered with noise from weaker players who are flush with cash and distort the price/value equation; a less competitive marketplace combined with lower costs of production should improve gross margin percentages of those companies with superior competitive positions and excellent operating teams.

Global opportunities for sales. If elected politicians globally can steer clear of creating a series of trade wars, middle markets should enjoy a great age of global market access and prosper disproportionately as the Fortune 1000 require much more time to fix potentially terminal issues.

"We think that the next two years will present themselves with some of the best investment opportunities we've seen in the last fifteen to twenty years," says James Marra, director of business development at Blue Point Capital Partners. "We have equity capital available and ready to deploy, we are reviewing as many qualified opportunities as we can, and we are hopeful that the additions to the portfolio this year and next will follow the pattern established by previous recessions, and result in high return investments over their lives."

To cite another Vegas-based film, we may be gathering for InterGrowth 2009 with a bit of "Fear and Loathing," but history and opportunity should reassure us that we have the resources, talent and wherewithal to make our own luck.



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