Lead Left Interview – Robert Gefaell

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This week we chat with Robert Gefaell, co-founder and partner, Plexus Capital. Plexus focuses on subordinated debt investments in middle market companies, with a total of $550 million under management across three funds.

The Lead Left: Robert, you and your partners got started together at the old Centura Bank, correct?

Robert Gefaell: That's right, Randy. We all worked for Centura Bank from the mid '90s through 2002. In 1995, Bob Anders – at the request of then bank President Kel Landis – was successful in establishing Centura's first licensed SBIC named Centura Capital. Ultimately Bob hired me, Michael Painter, and Mike Becker. That's how it all started.

TLL: And when did you all found Plexus Capital.

RG: Well, in 2001 RBC acquired Centura Bank and named Kel the first CEO of RBC in the U.S. Unfortunately in 2002 it was determined by RBC to harvest Centura Capital's portfolio which we successfully did yielding a net return to the bank of 14% over the 9 year period. Ultimately Michael, Mike, and I left and all joined other SBIC's in NC, but ultimately found our way back together with Bob and Kel (after they took early retirement from RBC) in the summer of 2005 for the formation of Plexus – we got the band back together!

TLL: I'm very familiar with the strategy of bringing bands back together.

RG: We then got our first SBIC license under the Plexus name, raised $27 million of private capital from 20 banks and 40 individuals, and ultimately funded our first transaction on December 30, 2005. With 2 tiers of leverage from the SBA, Fund I had $81 million of investable capital which was used to finance 28 companies over a 4 year period.

TLL: When did your second fund close?

RG: That was in 2010. We raised just north of $58 million, so with leverage we had a $175 million fund from which to invest. It also had, coincidentally, 28 companies in its portfolio. 2 years ago in May of 2013 we raised our third fund – we raised $150 million in private capital and plan on taking $150 million in leverage. To date we have invested $154 million of Fund III in 18 companies.

TLL: Because the SBIC caps leverage at a maximum of $150 million?

RG: That's correct. We are leveraging our Fund III capital calls on a 2 to 1 basis currently until such point we hit the cap on the leverage. Our LP's are still deriving attractive return enhancements from the leverage as we deploy capital in companies coast to coast.

TLL: How do you define the kind of companies you look for?

RG: We seek later stage, growth oriented businesses that have reached an inflection point in their life cycle where outside capital is needed. These companies typically have a great relationship with their existing senior lender, but have simply maxed out their ability to attract any more debt – that's when mezzanine debt most often comes into play.

TLL: I assume most of these companies are private.

RG: Correct, however; two of our existing portfolio companies are actually public. We target companies with revenues under $100 million and EBITDA under $20 million. Most importantly to us though is management: management, management, management! I would rather have an A-rated management team with a C-rated product/service then the inverse – products/services can be fixed, typically people cannot.

TLL: Most of your investments are in the form of subordinated debt?

RG: The vast majority for sure. Some unitranche and some equity as long as it's in concert with a larger mezz check from us.

TLL: Do you get upside with your mezz?

RG: Out of our 74 investments since inception, we have upside in all but 2, primarily through penny warrants, but also through equity co-invests.

TLL: How many companies are backed by private equity sponsors?

RG: Only 20% of our deals are sponsored-backed. While we like to see PEG deal flow, purchase multiples sponsors are paying today are incredibly high and we tend to get uncomfortable when being asked to get aggressive on leverage and frankly beat-up on pricing to levels that fall below our risk/return profile.

TLL: How aggressive are they being?

RG: I've seen deals where the purchase multiples are north of 9x EBITDA (with EBITDA in the $5MM range), pro-forma capital structures suggesting leverage through the mezz of 4x+, and all-in pricing in the 10%-11% range. If leverage is above 4x it's likely not a deal for Plexus. We feel much more comfortable with all-in leverage through our debt of 3.0x to 3.5x and pricing commensurate with the risk. And no, this is not a unicorn! We pride ourselves on staying in front of referral sources, staying relevant in the market, logging serious hours in cars, planes, and trains in order to turn over far more rocks then our competitors. We are not afraid of taking the road less traveled to find the best opportunities for the benefit of our investors.

TLL: How do you target opportunities?

RG: We look for entrepreneurially run companies, most of which have never changed hands, that have a growing business where the owner a) wants to take the company to the next level and needs capital to do so; or b) is seeking a liquidity event for all or a portion of their ownership – we can help them take some chips off the table.

To be continued the week of June 22

Contact:

Robert Gefaell
Robert@plexuscap.com