Lead Left Interview – William G. Winterer (Part 2)

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This week we continue our conversation with William G. Winterer, partner, Parthenon Capital Partners. Bill is head of capital markets and a member of Parthenon's investment committee. Parthenon is a private equity investment firm that has managed funds with over $3.5 billion in total capital commitment with offices in Boston and San Francisco and approximately 20 investment professionals. ***Second of two parts –*** ***View part one***

The Lead Left: What's going on in business services?

Bill Winterer: We like software-based businesses with recurring revenue models, high value propositions and mission-critical services. Who doesn't like those types of business? In any case, we try to leverage what we know to find attractive opportunities where we can be good partners.

Government services have been good for us. Also security and monitoring companies. There's a good value proposition there, as the industry incorporates more technology. The need for security everywhere, whether it be physical or IT-based, has increased. Certain niches within IT services. We believe we are particularly good at understanding and optimizing service-based businesses that combine of labor and technology.

TLL: What's your view of purchase price multiples? How do you compete at these levels?

BW: We certainly see high multiples and we pay fair and market prices. But our job is to make our LPs money. We try to differentiate ourselves from other buyers through our strategic vision, style and values, experience and resources. Whether a proprietary deal or a process, we try to bond with the management team and develop, on a collaborative-basis, a long term plan. This helps both sides to determine if there a good fit, so ideally a seller's decision isn't all about the highest price.

TLL: What's your add-on strategy with your portfolio companies?

BW: It's helpful to do add-ons, certainly. But more important is our investment thesis around the market growth and opportunity. We really like acquisitions that expand the portfolio company's addressable market. We're not doing roll-ups for roll-ups sake. It's all about building a strong and strategic asset. We've done approximately 100 add-ons within our portfolio over the last five years. Yes, they are often accretive, but the strategic vision, synergies and integration execution are the real value enhancers.

TLL: As head of the firm's capital markets practice, how do you see financing? What's changed?

BW: We've seen private credit funds emerge in a big way. There are a number of new players, some affiliated with private equity groups, some with insurance and pension companies like yourselves. They seem to have hired good people. Of course many of them don't have long track records but appear to be building sustainable and logical businesses.

TLL: You don't really know how they will behave in a downturn.

BW: No one knows. They should be smarter and more patient than regulated banks, but who knows? They're doing and saying the right things. We'll see how the cycle plays out. It seems like right now everybody is about flight to quality – debt and equity providers alike are chasing the same assets – given some of the macro-economic, global and political uncertainties. At Parthenon, we try hard not to be part of a herd mentality and rather be amongst first movers or figure-out misunderstood opportunities. Also some of our investments take a little longer than average PE to build and may hit "speed bumps" that require patience. We like to work with lenders that take similar approaches and can appreciate the time and effort we and management put into optimizing our portfolio companies.

TLL: Do you use unitranche financing for your deals?

BW: Yes and no. Out of our twenty financings – refinancings, major add-ons, and new LBOs – in the last four years, we've done two unitranche structures and they've made sense. We're open to it, will continue to consider it, but maybe we are a bit old-school. More traditional club and multi-tranche deals mean you get to touch more lenders which we think is a good thing longer term for our companies, management teams and the Parthenon franchise.

TLL: How about mezz?

BW: We haven't utilized mezzanine debt in about five years. We have used second lien debt with 9-11% yield. It seems like this cycle has been unkind to mezz, but I am sure things will change at some point in the future, like it always does. We generally like the fact that subordinated second lien debt isn't subject to 1st lien debt payment blocks during a technical default, as it gives the borrowers more control of payments vs the 1st lien lenders dictating a block.

TLL: You mentioned the cycle. Where do you think we are in this one?

BW: Look at history. Politicians have always tried to limit cycles. While attempting to limit the downside it probably also limits the upside. Today, there is so much government interference in our economy, it is hard to predict exactly where we are or what is going to happen. GDP has now been growing for seven plus years; based on traditional time thresholds we should be getting close to the end of this cycle.

Furthermore, two hundred years of US economic history have demonstrated that cycles are correlated to the end of eight-year Presidential terms. We don't have a crystal ball, but we're coming to the end of another one soon.

TLL: Bill, what's been your biggest surprise so far this year?

BW: How the market has bounced back since late 2015, early 2016. Think about where we were six months ago: the high yield market had effectively shut down, BDC values had plummeted, banks were out of the market, and fund flows had seen enormous outflows. The bounce back has been incredible. The speed of the recovery was certainly surprising to me.

TLL: You mentioned politics. Certainly some surprises there.

BW: Yes, I don't think anyone predicted Trump would win the GOP nomination, while Hillary struggled to put away Bernie.

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