Lead Left Interview – Paul Peterson (Part 2)

THE LEAD | August 9, 2016

This week we continue our conversation with Paul Peterson, a managing director at Wind Point Partners. Wind Point Partners is a private equity investment firm that with a strategic focus on facilitating leadership transitions by partnering with top caliber executives to acquire middle market businesses with a clear path to value creation. Since its founding in 1984, the firm has raised over $3 billion in commitments and acquired more than 90 platform companies and 160 add-on acquisitions. ***Second of two parts – View part one***

The Lead Left: Talk to us more about that third bucket?

Paul Peterson: Creativity creates change the market *doesn't* anticipate. For example, we are in pursuit of an opportunity right now where we are paying a market clearing price for a platform within a niche industry. On its own there are nice opportunities and we are partnered with a strong executive to take over the CEO role. But we are also in discussion with the #2 player in the same niche and have pretty unique insight into the synergies due to our executives knowledge of the business. Internally we call this connecting the dots, the more angles or value levers you can line up the more dots are connected and the more compelling a deal becomes.

Its pretty easy to have an operating partner sitting next to you and pay top dollar in an auction, but the third bucket is more challenging. I tend to think about it as finding value. There are the no-brainer deals that everyone wants to own and there are the no-brainer deals that nobody wants to own. The deals in between are where you need to connect the dots and find an angle.

TLL: Can you give us an example of an in-between company you've bought?

PP: PetMate, the financing for which Churchill participated in, is in the consumer products world, durables in particular. Petmate is a supplier of various pet products including injection molded and Asian sourced goods. There are not a lot of power house brands in consumer durables. On the premium end you might think of some recent deals like Yeti Cooler or Shock Doctor, these are pretty unique brands that a lot of investors would like to own. At the other end of the spectrum are consumer product companies that have or are at continued risk of disintermediation from direct sourcing by retailers, it's a difficult sell.

When we bought Petmate it did not have a CEO and the business had just recovered from a failed acquisition integration. So the story was challenging but underlying the noise was a fundamentally solid business and a stalwart in the pet industry. Petmate is the definitive leader in the pet space for injection molded products such as the classic kennel, shelters, feeding and water systems, and litter pans. We complement that with a full suite of Asian sourced products including branded toys. Ultimately we have a clear competitive advantage in a very fragmented market where retailers are increasingly looking to consolidate their sources of supply.

TLL: The premium consumer brands are certainly getting eye-raising multiples.

PP: True, strong consumer brands are incredibly valuable but they are in short supply and tend to elicit significant strategic interest.

TLL: Paul, what kind of things do you think about in terms of market trends?

PP: If you go to conferences, people talk about pricing, leverage, competition, and so on. The questions and answers are exactly the same thing as they were 15 years ago. When has it ever not been competitive? Never. It's a silly question. People are always complaining about valuation multiples and the number of firms competing for deals. That will never change.

TLL: So what does change?

PP: Over the last 15 years, we've seen an increasing focus on industry sub-sectors. There is real value in being deep in certain sectors. It was easier to pursue a generalist approach in the past. Now you're behind the curve if you're learning a sector or sub-sector at the beginning of a deal. It's very different when you know people and companies in the sector. If you have some domain expertise, that is a differentiator.

TLL: OK, Paul, what's been your biggest surprise this year?

PP: The first quarter was not an active deal environment; the second quarter has been very active. It's very interesting to watch how that level of activity has changed so quickly.

TLL: And what keeps you up at night?

PP: That's a good question. I wouldn't say it keeps me up at night but I think the potential for disruptive technology and business models is something that we need to start looking at more seriously in the middle-market. Middle-market private equity is not visionary like the Silicon Valley crowd but the pace of change is so rapid at some point we need to factor some of these risks into our exit multiples if not our typical 5 year horizon.

For example, in the industrial world, many businesses have at least some, if not significant, exposure to the automotive world. We all know the "pie in the sky" scenarios being painted right now relative to a world with a common fleet of autonomously driven vehicles at everyone's fingertips. That scenario makes sense from so many different perspectives and given the sheer amount of capital going into this effort it almost becomes self-fulfilling. And in this scenario the world needs far fewer cars. This is the type of issue that private equity investors might ignore as a 20 to 30 year issue. But its not hard to see a scenario where you make an investment today and in 5 years you exit and there is a huge impact to the exit multiple.

Contact: PaulPeterson
ppeterson@wppartners.com