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BUYOUT FIRM OF THE YEAR: The Riverside Company

Recipe For Success Gets Riverside Through Challenging Year

Step one: Hand-pick small companies that lead their markets thanks to compelling, unique products and services. Step two: Have operating partners give their management teams advice on how to compete more effectively. Step three: Double or triple EBITDA during a three to seven year holding period through add-on deals and organic growth. Step Four: Place in oven, and bake at 350 degrees for half an hour.

OK, forget that last step. But if you follow the first three, you'll have gotten a taste for the formula that's seen **The Riverside Company**, founded in 1988, rise to become one of the largest, best-capitalized buyout shops in the country focused on the small end of the middle market.

"It's a recipe that generates a pretty good cake every time," said co-CEO **Stewart Kohl** of Riverside's approach to small-cap buy-and-builds. "We're kind of the Duncan Hines of private equity."

That may be, but every so often a year like 2009 comes along, stressing even the most time-tested of recipes. The eggs get spoiled, the mice get into the cake mix, the oven goes on the fritz, and before you know it you're heading to the supermarket to pick up a pre-made cake. Kohl acknowledges that the past year presented plenty of challenges for the firm. Lowlights include a lifeless fundraising market, the Great Recession, and an M&A market with a shortage of healthy companies for sale.

But Riverside still chalked up impressive numbers. The firm closed a \$1.17 billion fund, beating its \$900 million target.

It closed 15 new transactions, six of which will serve as platforms for buy-and-builds. It scored four exits during the year, including one that produced the largest equity gain ever for the firm. All in all, the performance merited a "Firm of the Year" award from the editors of *Buyouts*, and leaves Kohl optimistic about Riverside's prospects for picking off some "wonderful companies" in 2010. But it wasn't easy.

Its coffers running dry, Riverside, which manages more than \$3 billion, set out to raise \$900 million for Riverside Capital Appreciation Fund V back in March 2008, according to *Buyouts*. It was not a propitious moment to ring institutional doorbells. The credit crunch that had started the previous summer was in full force, the economy was in recession and, before the year was out, the country would be in the grips of a financial crisis. Many investors, particularly endowments, were simply out of the market; those that had money to commit to private equity funds could afford to be highly discriminating.

Riverside's marketing strategy centered on "organizing a tremendous amount of data" to overcome investor objections and biases, Kohl said. These biases included a feeling among some investors that small companies suffer more in recessions than large companies do—true, perhaps, for a random selection of companies, but not for a Riverside portfolio, according to Kohl.

The firm also spent more time than expected courting new investors, particularly pension funds still enjoying cash inflows despite the financial downturn. In the end, about half of the money in Fund

SNAPSHOT:

Offices: 18 in North America, Europe and Asia, including New York, Cleveland, Hong Kong, Tokyo and Budapest, Hungary

Founded: 1988

Employees: 180

Assets Under Management: More than \$3 billion

Business: Through its "Capital Appreciation" family of funds, the firm acquires platform companies generating EBITDA of \$5 million to \$15 million and seeks to double or triple that figure during a three to seven year holding period.

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WHY THE FIRM WON

- Raised \$1.17 billion fund in difficult fundraising market, beating \$900 million target.
- Scored four exits during the year, including the estimated \$500 million sale of ATI Enterprises, a for-profit provider of career training that grew from under \$10 million in EBITDA to more than \$50 million during a nearly six-year holding period.
- By and large kept portfolio out of trouble in a tough economy, which enabled the firm to focus on completing 15 transactions, including six platform investments.

V came from investors new to Riverside, instead of the 25 percent Kohl would have anticipated under more normal circumstances. It took the firm about twice as long as expected to wrap up the fund, which closed after about a year in the market. "It was hard work," said Kohl. "But the silver lining is that we have new, additional partners."

Another significant achievement for Riverside during the year was keeping most of its portfolio of 70 companies



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on track. Naturally, the firm experienced some hiccups. Kohl said the firm made the “cold, rational” decision to pull its financial support from one company, and that in a handful of other instances, perhaps six or seven, Riverside had to sit down with lenders to deal with missed covenants.

But Riverside experienced no bankruptcies during the year. And the portfolio saw only a modest, mid-single-digit percentage drop in EBITDA in 2009, handily beating the performance of S&P 500 companies, according to Kohl. The 19 companies in the firm’s micro-cap fund portfolio, which typically generate less than \$5 mil-

lion of EBITDA when acquired, actually logged EBITDA gains on average.

The key to that performance, said Kohl, had been instructing management teams back in the fall of 2008 to expect the worse. Make deep cuts to protect EBITDA, Riverside told them, be thoughtful about the cuts to avoid undermining sales, and stay in the good graces of lenders. “Most or all of them today would say, “Thank you, that was the right decision,”” said Kohl. That would probably include the management team at Connor Sport Court International, a supplier of basketball courts and related sports flooring that generates about \$50 million

in annual sales. Anticipating that the cyclical business would take a pounding in 2009, the company took a number of cost-cutting steps. These included tightening up quality controls to reduce warranty costs, and moving to a production schedule better tuned to orders. As a result of these and other measures, the company saw EBITDA grow more than 5 percent last year, even as sales fell 13.5 percent, Kohl said.

Connor Sport Court took the steps it needed to survive a tough year. The same can be said for its parent, and no buyout shop tracked by *Buyouts* had a better 2009 than Riverside.—D.T.

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Riverside