

Providing Sellers Certainty of Sale with KPAC Solutions



Editor's Comments: Business cycles have transgressed from the popularity of the conglomerates during the 1960s when large companies were restricted from certain industry acquisitions because of the tough anti-trust laws at that time... to the halcyon years of the 1990s when growth through aggressive acquisitions was spurred-on by a stock market that rocketed to new highs year after year.

Now in the decade of the 2000s with heightened competition through globalization, companies, especially public entities, are taking a hardened and disciplined approach to their business units... frequently executing a "shrink, fix and grow" strategy. In this fast moving business environment, respectable profit growth is often achieved by shedding the least profitable businesses and focusing on a few core areas.



Jim Patton

The stage is now set for this article. The message is that unprofitable businesses that can not be fixed should be sold so that management can devote its time, effort and capital to its profitable entities. But what if these unprofitable businesses are not sellable through the normal auction process orchestrated by investment banking firms or directly by the parent company? Then what? The answer often is to contact KPAC Solutions, the subject of this article.

OVERVIEW

KPAC, LLC is a private equity group that acquires deeply troubled companies, preferably divisions of public entities or private equity groups, and very quickly restores them to profitability and resells them historically with the average ownership period being 2 years. KPAC's industry focus is manufacturers, distributors or construction companies with minimum revenues of \$10 million to \$100 million, almost always with negative EBITDA, negative trends, limited technology advantages or lack of a global focus. Usually when KPAC enters the scene, others have tried and failed to sell the distressed company and/or no one else has the capability or desire to undertake such a transaction. An important distinction in KPAC's *modus operandi* is that the distressed company must have audited financial statements, because their offer is largely based on the accuracy of the reported numbers. Furthermore, KPAC almost never acquires companies in bankruptcy partly because of the speed in which they operate: (1) purchase price and terms offered in 3 days from receiving the Selling Memorandum; (2) followed by a Letter of Intent (LOI) within the next 10 days and; (3) concluding with the transaction closing 30 days after acceptance of their LOI.

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EVOLUTION OF KPAC

Like many success stories, there is often an entrepreneur who starts from a modest business background. Jim Patton from the Nashville, Tennessee. Upon meeting him, one can not help but be impressed with how he carries his 6'4" frame. At age fifty, he impresses one with his erect but thin posture, set-off with his pure white mustache and head of hair. Asked how come his hair turned white at such a relatively early age, he replied: "Stress! In the much earlier days of KPAC, I was meeting payrolls every Friday when there was no money in the bank on Wednesday!"



In his original business career, Patton worked as an electrician and eventually as an Industrial Engineer for Rohr Industries, located in Winder, GA. In 1992 at age 35, Patton acquired an underperforming job shop. While he was able to turn the business around, he had run out of cash principally because he overpaid for the company where he was obligated to pay a royalty on sales (the better he did, the more he had to pay). Two years later, he had to turn the company back to the original owner. As Patton said: "It practically killed me to relinquish the business after I had turned the business around. One really learns from a bad deal... it made a lasting impression on my deal structures going forward, that is for sure."

Over the ensuing decade, KPAC has acquired 13 platform companies (almost all from Public Companies), successfully selling all of them (3 back to their owners), leaving KPAC with one remaining portfolio company. KPAC's team of experienced managers gives them the ability to handle worldwide distressed companies expeditiously. Cited below are the key individuals.

* Kevin Kennedy (Virginia)	Former President & CFO for both privately held and public companies with revenues ranging from \$20 to \$250 million
* Fil Filipov (Paris)	Former CEO of Terex Cranes EVP of Clark Material Handling Co. VP of J.J. Case Co.
* Bob Gielow (California)	Former senior financial officer for Kinko's Inc. VP of Finance Print Technology, Inc. CFO for PlayStation America and Cash Technologies
* Leon Deutsch (Iowa)	Group President of Terex Cranes President of Waverly
* Rob Shuler (Tennessee)	Managing Director of two investment banks, Market Street Advisors and USBX CFO of Gold Leaf CEO of Petra Capital

The team of six members consists of a lead negotiator (1): Patton; turnaround experts (3): Kennedy, Filipov and Deutsch; a senior financial officer (1): Gielow; and a marketing/deal originator manager (1): Shuler.

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An important part of KPAC's deal team is KPAC's attorney, Michael Hinchion, located in Nashville, TN, from the 200 person law firm of Stites & Harbison headquartered in Louisville, KY. KPAC and their attorney work at lightening speed and are very focused towards moving the deal to closing, i.e., 3 days to submit a two page offer, 10 days to submit a binding LOI; and 30 days to close. KPAC is willing to acquire the distressed company at near book value but without interest bearing debt, lawsuits (actual, threatening or pending), and environmental problems (will acquire but with full identification of the Seller). Under these conditions, KPAC focuses on the major assets: plant, machinery and equipment, accounts receivable, inventory, work-in-process and will not "cherry pick" these assets during the acquisition process from the seller. KPAC will consider acquiring the stock or the assets of the company in a transaction."

POST ACQUISITION

The game plan in the first 100 days is to shrink the business by eliminating the unprofitable product lines and/or unprofitable customers. Then KPAC consolidates core products utilizing the old 80/20 adage, i.e., 80% of the sales come from 20% of the products and 20% of the customers.

The game plan is to cut the SG&A immediately, impose strict disciplines on purchasing with all orders over \$100 needing authorization. Headcount reductions are usually done very quickly after the acquisition. Turning to the vendors, KPAC often expects them to cut their prices by some margin to keep the business, noting also whether they have delivered on time and whether they charge for freight. KPAC's goal is to eventually become the industry's low cost producer. KPAC almost always cuts the prices to the customer base through aggressive internalized cost reductions.

As Patton explains: "From day one we bring back life into the workforce, we give them confidence and substantially increase the morale. Ironically, 90% of the time, management under the CEO level knows the answer to the company's problems, but they either do not have the ability or the authority to correct the situation. We go through a 100 day immediate reorganization where we shake the company down to the core. If the company has multiple plants, we might close a few and consolidate them. Many of our companies are subjected to industry overcapacity such as automobile parts, printing, fertilizer manufacturing, etc., and other companies that are severely impacted from foreign competition such as textiles, resins, steel, etc."

Patton continues: "After 100 days of very intense turnaround work and basic "blocking and tackling," we are in a position to grow the business organically. While we have never had a failure, there are always surprises, and sometimes the company takes a turn for the worse right before our acquisition. We will close anyway; with modest, fair changes to the acquisition agreement. KPAC doesn't bait and switch with the seller during these stressful negotiations. Within a year's period, we may be ready for a bolt-on acquisition to increase the critical mass. Our goal is to double or triple sales and to re-sell the company when earnings will be accretive for the new buyer... usually the dominant player in that industry, which is often a public company. Our exit strategy is almost always to a public company with a selling price at some fair multiple of established earnings, bringing KPAC a handsome profit."

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ADDING VALUE TO ACQUISITIONS

Example of Typical Acquisition's Metrics

At Closing Revenue	At Closing EBITDA	After 12 Months Revenue	After 12 Months EBITDA	Year 2+ Growth Rate
\$30 million	(\$1.5m)	\$22m	\$1.5m	20%

Categories for immediate EBITDA improvement:

- Discontinue unprofitable product offerings
- Reduce labor
- Consolidate facilities
- Improve purchasing

CONCLUSION

In a recent article published by *Investor's Business Daily* and written by Jerry Jasinowski, he expresses his concern about the future of America's manufacturing base and their ultimate survival. "Many manufacturers are plagued by high structural costs which squeeze profits and undermine companies' ability to invest, innovate and create jobs. Profit deterioration is frequently due to higher health care and pension costs, which are particularly onerous for domestic manufacturers with large retiree populations. Other drivers of the profit squeeze are high energy costs and misaligned exchange rates that drive up material costs. Excessive costs – coupled with unfair trade practices such as China's currency manipulation – make it extremely difficult for U.S. manufacturers to compete and, in some cases, threaten their very survival."

Based on the above observation by Jerry Jasinowski, an economic and president of The Manufacturing Institute, it would appear that KPAC will be very busy in the years to come. KPAC's record shows that they have completed 13 platform acquisitions in 12 years both here and in Europe, of which they have exited 12 successfully, while currently managing one portfolio company with manufacturing assets in the United States and Europe along with distribution facilities reaching to Asia.

Patton ended the interview with *M&A Today* by saying: "We're the quiet company, not many public companies know about us or our aggressive acquisition strategy for distressed companies and their assets, but those who have dealt with us are very glad we quickly came to the table like we did. With more busted auctions and breakdowns in transactions taking place these days, KPAC is standing ready to quietly but quickly take a troubled company off the Seller's books."

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