

Ben Mackay of Evolve Capital

[00:00:04] This is the Investor Connect podcast program. I'm Hall Martin and the host of the show in which we interview Angel Investors, venture capital, family offices, private equity, many other investors for early stage and growth companies. I hope you enjoy this episode.

[00:00:24] Hello, this is Hall Martin with Investor Connect. Today, we're here with Ben Mackay, principal at Evolve Capital. Evolve Capital is a private equity firm focused exclusively on leveraged recapitalizations of entrepreneurial businesses to provide entrepreneurs with liquidity up front and also upon exit through their retained equity stake. In between, they provide professional management and strong partnership, which increases shareholder value and attracts more potential buyers through entrepreneur management. Team partners focus on positioning companies to maximize value upon exit.

[00:00:51] Ben, thank you for joining us. Thanks for having me. So so what was your background before investing in early stage companies?

[00:00:58] I got kind of a long, varied background. So it's interesting. I let's see, I was I was actually a guide in Alaska for quite a while and ended up back at business school. And then after business school, I was living in Jackson Hole, Wyoming, flying paragliders and then ended up doing small business lending for Wells Fargo loans of twenty five million and smaller. And then I ended up meeting the principal at the time at Evolve and they asked me to come down to Dallas and that's really how I got started. And that was back in two thousand, seven or eight. And since then we have I'd say we've averaged probably one or two acquisitions per year. And we've got a long history in health care services. Probably about half of our portfolio typically is Medicare or Medicaid reimbursement, health care, hospice, behavioral health type businesses. And then we also have some specialty manufacturing and then generally sort of business services type companies. So one is a clean room cleaning business, very critical environment, cleaning business. And in the past, we've had other things like on the manufacturing side, like power management components, highly engineered, smaller components. We had a bottle ceiling and capping machine business that's old predominantly into the craft beer industry. So we are really all over the map. And I'd say at this point, we invest our own money in these deals

and we don't have a defined period. And we really enjoy working with founders of businesses and it's always a unique group of people.

[00:02:35] Great. Well, thank you for that. So what excites you right now?

[00:02:38] It's a it's definitely a shifting landscape. I think when covid had a lot of things, the brakes were hit a little bit on a lot of deals. I think now thankfully, we've seen certain parts of the economy come back well and others just because of the sort of customer dynamics that have been created by covid. There are other other parts of the economy that aren't going to be doing well, like restaurants, for instance. We've never really been involved with restaurants or construction or real estate. So I guess what I long story short, I think I think there's going to be some good deal flow coming in twenty twenty one. I think there's going to be some really good activity, particularly with the administration change potential increase in taxes. And I think me a lot of motivation for know founders or owners of companies who need a liquidity event or a transition or trying to work on an ownership transition to come to the table and and look for partners that are that are excited to kind of pick up the ball and run with what they've created.

[00:03:40] Great. So what's your advice for people investing in startups? What do you tell them to do before they write that first check?

[00:03:48] As far as investing in startups? I'd say for us we're a little later stage than a startup, more sort of five million revenue to maybe thirty million in revenue, one to five million of but so established business has been around for a while, has it has a track record. But I'd say one of the big things a lot of people think finance is all about the numbers and private equity is all about the numbers. And I'd say, you know, it's really more about the people and making sure you set up a partnership we call called a partnership, because we always our deals always have the founders of the sellers retain ownership with us. And so you just want to make sure that the deal is set up where everybody's motivations are aligned and the seller is excited to to continue to be involved and say that's one of the biggest the biggest starting points. Right.

[00:04:39] And then on the other side of the table, what's your advice for people running startups? What do you tell them to do?

[00:04:44] I think one of the biggest things is you want to have you want to think about what your end game is from. So where do you want to end up? And I think that can be really helpful. Even talk to private equity guys and buyers and companies. Well, hey, what are you guys looking for? What does it need to look like? What are the key dynamics around a business that you look for when you're thinking about investing or buying a business? And and if if the if the founder can kind of sort of steer their company into the some of those aspects that make it attractive, then it just really helps.

[00:05:19] Right. And so let's talk about the state of private equity in. Seeing how do you see the industry evolving here?

[00:05:26] Well, there's been a I think the biggest one of the biggest dynamics that hasn't really been talked about, at least from what I've been reading, is with covid, there were probably a lot of businesses that got hit pretty hard. And there's been a trend of sort of independent sponsors for a long time coming up. And I think that I think that dynamic is going to be tested a little bit. The independent sponsor will be tested a little bit now that everybody's had to kind of dig in. A lot of lenders have had to step up and kind of support businesses that may have been sort of lightly supported by the original independent sponsor. For instance, there's been a lot of pain out there, really for people that were already invested in companies. And I think I'm guessing that the private equity world might shrink a little bit of the buyers, kind of the real buyers that are left standing and to stick around and the folks that want to do kind of one off deals or just one by itself. You might be met with a little bit more scrutiny by sort of finance and community. That's something that I think might start to exist. And other than that, like I said, I think I think the volume is going to be up.

[00:06:32] We've talked a little bit about your criteria, but can you flesh out and tell us more in detail about your investment thesis?

[00:06:38] Yeah, so so we target a size range, sort of like I said, that five to 30 million revenue, sort of one to five million EBITDA or cash, close range. We target that range because over our experience, which is more than 20 years, we found that when a company reaches that size range, it has a critical mass. They probably have somewhat of a management structure and they built a business that that is probably hopefully sustainable. So it's got some real weight behind

it, but it hasn't reached the level where they've had to build maybe a build out their sales team extensively or they may not have a CFO, for instance. And it's at that stage where our founder or the owner of the business is probably wearing like five or 10 different hats. And they are probably doing a number of things that they that they don't really want to be doing. And they maybe have gotten away from the things that they they they love to do, which is why they got into the business in the first place. And so that allows us to step in with our area of expertise, which is helping to pull some of those tasks off of the founder's plate and take them on to ourselves and allow the founder and the seller to get back to what they love doing most. And when you do that, that really sets the business up to scale more efficiently. So when people are doing things that they want to do, they're excited about and doing less of what they're not excited about. It really it sounds really simple. It's not it's actually difficult in practice. But when it when it works, it works really well to grow the business.

[00:08:17] Right. Can you talk about a startup that fits that thesis? Oh, man.

[00:08:21] They're all there. We've got a lot of them. Let's see, so, for instance, the I would like to talk about that bottle filling and capping machine company, so they had six employees when we bought them, they were like 15 million in revenue and three million in cash flow. And the question that's a very fine management team and enable a scale that we had to bring in some our resources, build a sales team. And we also had to look at add on acquisitions to diversify the customer base as well. So, I mean, I think that's maybe one example.

[00:08:58] Good, good. So good. With a lot of startups and investors in today's world, what do you think the main challenges today for the startup? What do you see them spending most time struggling with founders and sellers?

[00:09:11] I think I think in our size range, they are struggling with that. It's a classic issue there. They're trying to do too much. They're not willing to delegate enough and take our hands off the reins. And a lot of times maybe they don't want to take on the headaches of hiring more hiring and managing more people they like. A lot of times, founders like they like the front end, the sales side of the business. They don't like the finance in the H.R. and the you know, the other stuff, more mundane business management side of things. And so I see people kind of getting into that rut where they're just. Buried under the weight of everything they've had to

take on to get the business to the size that it is and to just make that leap to the next level, it's sort of daunting to think about. OK, well, how am I going to run a process to go hire a general manager that can handle all the stuff that I do right now and that kind of question? And that's what we can create.

[00:10:09] And then on the other side, what is the main challenge the investor faces in today's market?

[00:10:14] That's a good question. There's so many in terms of just finding a good fit. What I think is finding is so finding a good fit, which which I don't necessarily mean business. I almost I really mean sort of a personality with the founders and the owners and starting off with a good personality fit and then working through a deal is that that's sort of the bread and butter, the basics, my opinion. The rest of it flows from there, I'd say. Like I said earlier, you know, the due diligence side of things, it's so helpful if the owner has a a feel for what we're looking for in there in in their business. So can you produce regular monthly financials, just kind of getting that business ready for sale? We are ready for a liquidity event. There's just some classic things that need to happen. Which one is having a good time with financials and setting up your. Org chart the right way, thinking about what your post closing role might want to be, what's your dream for what you want to do afterwards? How do you want to be involved or not involved with those kinds of questions are important to think about. Right.

[00:11:24] But you've talked about several sectors and applications. But if you had to pick one or two that you think are good immediate opportunities for investors to pursue in today's economy, what would you put at the top of the list?

[00:11:34] My Holy Grail type of business is a it's a company that would be a manufacturing business that makes components, highly engineered components of components that that require a degree of engineering specialty that that are then used in a critical environment. And and ideally, those components on a per per unit basis are relatively inexpensive. And by that I mean maybe five hundred thousand five hundred dollars to three thousand dollars somewhere in there per unit on a business that's making five or 10 million in revenue. What that means is it's a it's a critical part that is hard to replicate. If they have an engineering company, they probably have some IP related to it. So there's some barriers to entry and. Then it's being used

in a critical environment, so so at a relatively low price. So your customer is not going to take a chance on buying another part. A different kind of part if your part is already working and it's not that expensive. For instance, we had a business that made AC DC power to bring equipment for commercial ships and the units cost maybe five hundred thousand dollars each, but they're essential in converting electricity from for use and onboard power. And so nobody is going to cut you out in a budget process. That's something that's so essential and so inexpensive. A five hundred dollar part and five hundred thousand or a million dollars or more.

[00:13:05] Great for the last few minutes that we have here, what else should we cover that we have it?

[00:13:09] Well, for me, one thing I always like to lay out there is I'm always I like to really put myself out there as a resource for founders and owners of businesses that have questions and or are curious about how private equity works, the dynamics and anything like that. I just I love talking about it. It's what we do. It's what I do all day. So, one, I'd like to put that out there. That's it doesn't need to be like a black hole sort of unknown area. There's certainly some unique dynamics that are classic in what we do and what what my colleagues do in their firms. And I'd be happy to talk about it with anyone about that. And then maybe it's a little self-serving, but always looking for great opportunities. So I guess by the same token, you know, I'd love to hear if anybody has any opportunities out there that I think they might fit in that sort of one to five million dollar range. That could be interesting.

[00:14:00] Great. Well, so how best for listeners to get back in touch with you?

[00:14:04] I think email is probably best these days. My emails just then evolve capital, dotcom and pretty much on it all the time and I try to be relatively responsive. Yeah, great.

[00:14:18] Well, thank you for taking time to join us today and hope to have you back for a follow up soon.

[00:14:22] Absolutely. Thanks for the opportunity.

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