

Buyouts

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FIVE QUESTIONS WITH...



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1 American Capital Strategies is one of the most active lenders in the buyout industry, so you see all kinds of deals. How close are lending levels and leverage multiples to all-time highs?

We're still quite a ways from the leverage levels of the late '80's, when leverage got to eight to nine times EBITDA. S&P reports current average leverage of about four and a half times but I think we all feel like it's more than that and our done-deal database bears this out. It shows average leverage levels of around 5.5x for sponsored middle-market deals. While that's not a record, it's quite high by historical standards, and most people feel like it can't go much higher. But, again, we've all been wrong before.

2 How much pressure is American Capital Strategies feeling from new lending players such as hedge funds?

There is tremendous liquidity across the capital structure, as we all know, and there's been record fundraising for private equity firms and record flows into a whole variety of leveraged finance vehicles. That said, the market has always been competitive, and I've never known a time when people weren't saying there's too much money chasing too

few deals. The key to our success in a competitive market is seeing as many of the opportunities in the market as possible and continuing to exercise good investment judgment and using our competitive advantages to win the deals we like. If we do that, we'll continue to be successful no matter who we compete with.

3 Are buyout firms in danger of overleveraging companies?

No doubt, some of the deals getting done today will be tomorrow's workout opportunities. We have had 3 or 4 years now of favorable economic, interest rate and lending conditions, and all the liquidity in the market makes some degree of over-leveraging almost inevitable. While we've seen many deals that have been too levered for our appetite, we continue to find opportunities with appropriate leverage, and we haven't seen a material increase in average leverage in our portfolio companies.

4 As a publicly traded company, do you have advice for any of your buyout industry brethren interested in raising capital through public markets?

If you assume they don't want to do it the easy way and just partner with American

Capital, my advice would be to study the models that have and haven't worked, and see if they can find one that works and fits with their firm. There's a growing body of listed private equity firms and asset managers around the world you can learn from. We think our public structure is a superior model in many ways, but you have to put all the pieces together to make it work. You need scale to bring analyst coverage and liquidity in the stock. You need a way to pay a dividend that's consistent and growing and at a premium to book value. You need an infrastructure to comply with Sarbanes-Oxley and all the other things that go along with being public. And you need a willingness to be transparent about your portfolio and operations.

5 When you go to a theater, do you always sit in the mezzanine?

That depends on who I'm with since I usually sit where other people want me to—my wife likes the center orchestra and my teenage daughters just want me as far away as possible. When it comes to sponsors, I'm happy to sit anywhere in the mezzanine, in the rafters with the senior lenders or in the front row next to the sponsor as an equity co-investor. ❖