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BUYOUT POINT OF VIEW: Accel-KKR managing directors Tom Barnds, left, and Ben Bisconti, talk about the upside of buyouts for the tech industry.

Accel-KKR eyes mid-market tech firms for acquisitions

Menlo Park's Accel-KKR LLC, a tech buyout firm, was founded six years ago by buyout giant Kohlberg Kravis Roberts & Co. (KKR) and venture capital firm Accel Partners. The two firms invested in Accel-KKR's first fund, estimated at \$300 million, and over the past three years, it has made seven investments. The firm specializes in buyouts of divisions of public companies, acquisitions and recapitalizations of private companies and taking small public companies private. Its investment committee, which vets all transactions, includes famed KKR founding partner Henry Kravis and Accel managing partner Jim Breyer. Accel-KKR's two managing directors, Tom Barnds and Ben Bisconti, recently sat down with Business Journal reporter Laura Cutland to talk about the climate for tech companies and why buyouts might be a good option for them.

Q: Why target tech companies in the mid-market?

Mr. Bisconti: There's not an industry around what we do. We think there's a gap. You have the traditional venture capital and growth equity worlds; you have the large buyouts, including increasingly the large tech buyouts; and then you have the IPO market. In between those worlds, you have companies in tech that have \$25 to \$125 million in revenue. They're too small to go public, maybe not growing fast enough to be interesting to the venture capital and growth equity worlds—and by that we mean sub-30 percent growth... That's a business for us.

Q: What tech sectors are most ripe for buyouts?

Mr. Barnds: Software and tech-en-

abled services. We think software is ripe today; it has been for the past few years and we expect it to continue because it's maturing. The growth rates have come down in general from 20 percent a year to 10 percent a year to now the high single digits. The economy is growing at 3 to 4 percent. So that for us is an attractive market. It's more mature; you have fewer new entrants and so future cash flows can become more predictable.

Q: Do you think buyout firms will ever get into life sciences?

Mr. Barnds: It's a volatile sector. You see fortunes made or lost depending on whether a drug makes it to a Phase 2 or Phase 3 clinical trial and ultimately to the market. I think that's a risk profile that most traditional buyout firms are unwilling to take. It has too binary of an outcome. It either works or it doesn't work.

Q: Why should a tech company consider selling part of its business to a buyout firm?

Mr. Barnds: It's a tough time to be a small public company. You have \$2 to \$5 million in incremental costs related to Sarbanes Oxley. So there are some costs you can eliminate by going private. Also, if you're a company that needs to undergo some transformation, you can make that transition out of the public light... And lastly, those closely-held private companies that many times are founder-run with a small group of investors—we can provide liquidity for folks where they might not otherwise have a path to liquidity because of the size you need to get to become a public company today.

INTERVIEW: While buyouts are hot today, keep in mind that these trends change over time

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Q: Buyout firms have been raising record amounts of capital in the last couple of years — perhaps more than they raised throughout the entire 1990s. What's going on here?

Mr. Barnds: Sarbanes Oxley is certainly contributing to the going-private trend. I don't know that that can be underestimated. When you're actually talking to CEOs and board members of public companies, there's frustration in how some of this is being implemented and, at some companies, you see fatigue. And when you have both of those coming together with a stock price that may not reflect the long-term value of the business, conditions are ripe for going-private transactions. So it's this environment combined with access to financing. The debt markets are certainly robust right now. The interest rates are pretty friendly. In effect, it allows you to have bigger checkbook when you're looking at these compa-

nies. Whereas a \$5 to \$10 billion tech buyout might not have been thought of much five or 10 years ago, you're certainly seeing them today. There's a partner at a large buyout firm that says in the next 12 to 18 months you'll see a \$20 million technology buyout, which is staggering.

Q: Some think this flurry of activity won't last and that buyout fundraising will eventually head into a down cycle. Do you agree?

Mr. Barnds: Certainly, there's a lot of capital flowing in but there's an awful lot of businesses out there — there are tens of thousands in technology — and there are an awful lot of businesses that can be run better.... In technology, the capital flows are much smaller — 3 percent to 4 percent of the dollars that go into buyouts. So it's still early in the game for technology buyouts.

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