

Deal Focus: Insight's First Deal is a Real Gas

BY ALEX J. STOCKHAM | A debut deal is always an exciting event for a new private equity firm. Making your first deal in the tough energy sector only elevates that excitement.

But investing in tough deals is exactly the way Southlake, Texas-based Insight Equity likes it. The recently formed turnaround firm's first acquisition of Direct Fuels from FFP Marketing shows the firm has hit the ground running, showcasing its specialty of acquiring struggling companies or corporate orphans.

Insight Equity was founded in 2002 by managing partners Ted Beneski and Ross Gatlin, both former Carlyle Management Group founders, and Victor Vescovo, a former principal at Bain & Co. The firm focuses on investing in underperforming, asset-intensive businesses with less than \$500 million in revenues.

Insight Equity's first deal hit that sweet spot, according to Gatlin. Direct Fuels, a gasoline distribution and wholesaling business, had approximately \$220 million in revenue in 2002. Not too bad for a business that didn't really exist five years ago. PNC Bank helped finance the deal by providing \$20 million in term and revolving credit. Gatlin adds that Insight was able to renegotiate the price to 15% below its original offer.

"PNC financed the deal in the middle of a war that had an energy flavor to it," Gatlin says. "That's a big win."

FFP Marketing's business was largely centered around owning convenience stores with gas stations. Direct Fuels was just a subsidiary. FFP began to think about strategic alternatives for the business and Insight Equity became involved before the private equity firm was officially formed. Gatlin was brought in by FFP Marketing's chairman and chief executive

An investment in a fuel distribution spinout shows promise in Texas

officer John Harvison to begin evaluating those strategic alternatives for the business. During that time, Gatlin and Beneski formed Insight Equity. The opportunity to help FFP Marketing remained on their radar, and Insight Equity became the preferred buyer of Direct Fuels. Insight and FFP entered serious discussions about the business at the beginning of this year, according to Beneski.

Direct Fuels operates a "terminal" facility in the Dallas area. For this part of the business, the company receives fuel from a pipeline, stores it in giant storage tanks, and sells it to end users who pick it up directly from the storage facility. The facility's end customers are typically un-branded gasoline retailers, like warehouse clubs and smaller gas station chains. The terminal sits on two pipelines, the Eagle and Explorer Pipelines, which provide 3% of the nation's fuel, and are connected to the facility's storage tanks.

The company's "wholesale" facility purchases gasoline and diesel fuel from various sources in Texas and arranges delivery to wholesale users, such as construction sites, docks, and fleets who need their own supply of gas.

Gatlin also is excited about the company's ethanol fuel additive business, which is becoming increasingly important on the U.S.' energy landscape. The company's small ethanol refinery and storage tanks sit directly adjacent to a rail spur for easy delivery to end users. Because of ethanol's rela-

tively short shelf-life, trains are the best delivery method, Gatlin adds.

All told, Direct Fuels supplies 75% of the Dallas-Fort Worth region's conventional, unbranded gasoline.

"Direct Fuels is a distribution type business, which we have experience in," Gatlin says. "It's firmly in our target segment, being asset intensive with revenues below \$500 million."

Direct Fuels was a relatively healthy company that suffered slightly because of some problems FFP Marketing was experiencing. Despite its health, Direct Fuels was still having difficulty getting credit.

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Of course, merely acquiring a business is not enough to guarantee a successful investment. Real work needs to be done. So, Insight's team got down to business by taking on operating roles at Direct Fuels, a bit of an unusual occurrence in the private equity realm. Beneski is now Direct Fuel's chief

executive officer, with Gatlin serving as chief financial and restructuring officer. Vescovo is the company's chief operating officer. The Insight team will remain in their operating roles for at least six months.

"We're managing the cash on a daily basis," Gatlin says. "We're managing customers on a daily basis. We signed the president and general manager to long-term employment agreements."

Other changes Insight has brought to Direct Fuels include moving the business to a new headquarters,

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Financial Sponsor Backed Acquisitions

July 2003

This chart displays the number and value of global financial sponsor backed acquisitions during July 2003, according to Capital IQ. The data is divided by sector and presented as buyout-only, venture capital-only and total deals. Values are in \$mil. Learn more about Capital IQ at www.capitaliq.com

	No. of Buyout Deals	Value of Buyout Deals	No. of Venture Deals	Value of Venture Deals	Total No. of Deals	Total Value of Deals
Energy	1	\$119.00	20	\$436.30	21	\$555.30
Materials	13	\$692.59	34	\$180.33	47	\$872.92
Industrials	25	\$393.07	52	\$1,627.43	77	\$2,020.50
Consumer Discretionary	15	\$1,726.38	29	\$903.71	44	\$2,630.09
Consumer Staples	3	\$0.00	2	\$9.32	5	\$9.32
Healthcare	2	\$0.00	40	\$1,075.02	42	\$1,075.02
Financials	1	\$0.00	12	\$706.71	13	\$706.71
Information Technology	10	\$132.50	130	\$1,219.76	140	\$1,352.26
Telecom Services	n/a	n/a	n/a	n/a	n/a	n/a
Utilities	1	\$335.00	2	\$7.60	3	\$342.60
TOTAL	71	\$3,398.54	321	\$6,166.18	392	\$9,564.72

2003 Year-to-Date

	Total No. of Deals	Total Value of Deals
Energy	130	\$5,606.09
Materials	342	\$10,708.24
Industrials	562	\$27,153.17
Consumer Discretionary	357	\$33,172.32
Consumer Staples	53	\$1,393.00
Healthcare	341	\$5,327.06
Financials	102	\$7,546.41
Information Technology	909	\$10,234.20
Telecom Services	21	\$154.22
Utilities	11	\$490.52
TOTAL	2,828	\$101,785.23

2002 Totals

	Total No. of Deals	Total Value of Deals
Energy	226	\$7,405.48
Materials	652	\$27,862.68
Industrials	1126	\$42,453.20
Consumer Discretionary	707	\$45,297.57
Consumer Staples	77	\$2,224.15
Healthcare	626	\$13,525.36
Financials	200	\$12,342.62
Information Technology	1711	\$19,068.81
Telecom Services	41	\$3,417.11
Utilities	21	\$1,622.33
TOTAL	5,387	\$175,219.31

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retaining key members of management, and getting new customers and vendors. Gatlin adds that the business has now been able to establish \$4 million in trade credit, which it didn't have when Insight bought the company a few months ago. That trade credit has boosted profits already.

Insight has also changed the

employee health and benefit programs to build morale among the employees. Gatlin says they've also established a new incentive system so that when EBITDA goes up and debt goes down, employees get paid more.

"That motivates the employee base so they can drive value and get paid for it," Gatlin says.

With all of these improvements -

and a simple change of ownership - Direct Fuels should see some solid results. Gatlin says he believes the firm can help the company significantly increase its EBITDA over the life of the investment. He also believes Insight Equity can achieve an outstanding IRR on their investment, something the firm's investors should find very interesting.