Buyouts

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For Saul Fox, Bigger Isn't Always Better in the World of Buyouts

By Leslie Green

Saul Fox, chief executive officer of **Fox Paine & Co.**, knows what it's like to be the big fish in a small pond, but he also knows what it's like to be a significantly smaller fish in a continuously growing pond. And he'll be the first to let you know, he prefers being the small fish, hands down.

His career as a private equity professional began with an invitation to join **Kohlberg Kravis Roberts & Co.** in 1984 – the biggest fish of them all.

From Law to LBOs

Fox had been working as a tax lawyer for Los Angeles law firm **Latham & Watkins** since graduating from the University of Pennsylvania Law School in 1978. He claims to have loved tax law (for some strange reason, he says), probably because his father was an accountant, but notes that his early years at the law firm were significantly more meaningful because of his participation in firm management and the opportunity to work with big-time clients that included the pioneering KKR.

He was moving right along in the world of law when Latham asked him to open an office in Chicago in 1984. That of course would have required a big move, Los Angeles to Chicago, but Fox jumped at the chance, realizing he would be closer to his most prestigious client, New York-based KKR.

Ecstatic over the news, Fox called his friend and client **George Roberts** to tell him how beneficial it would be for Fox to be closer to New York, but as soon as the words were out of Fox's mouth, Roberts said, "Don't do anything yet. I'll call you back in half an hour."

Thirty minutes later Roberts and Fox were once again on the phone and by the end of the conversation, Fox was no longer on his way to opening a law office in Chicago. Roberts had offered Fox a job at KKR that he couldn't refuse.

He saw the opportunity to join KKR, and its then novel approach to investing, as a challenge, he says.

"I started to find the business

issues that my clients were working on more thought-provoking than the legal and tax issues that I had been focusing on as a lawyer," Fox says. "So when the opportunity presented itself to join the business side, I ultimately thought it would be a greater challenge and that appealed to me."

Fox stayed with KKR for 12 years. He says three deals in particular stand out to him as the most noteworthy during his tenure with the New York firm: **American Reinsurance Co.**, the largest insurance company LBO to date; **Canadian General Insurance Group**, KKR's first international LBO; and **Motel 6**, a chain of budget motels.

Fox was the KKR partner in charge on all three deals, which returned $3.1 billion in cash for a 52% internal rate of return.

Although many investors consider George Roberts a model after which they have shaped their careers, probably only a handful can truthfully call him a personal mentor and friend. Fox is among those few.

Mogul Mentor

"He allowed me a lot of rope in the sense that he wasn't controlling all my decisions at KKR," Fox says of Roberts. "He allowed me to be as independent as I felt comfortable. When I came back to ask questions or talk about a deal I was working on, he always asked the questions that I wasn't necessarily thinking about."

Fox also says Roberts taught by example versus teaching solely by direction.

"He is intelligent and dispassionate, not emotional, in his business analysis, and I admire that," Fox says. "He has influenced who I am as an investor more than anyone else in the business."

Back to Basics

But despite the high-profile deals and being "monstrously overpaid" at KKR, Fox got the itch that made him want to move on to something different.

In the mid-'90s, as firms like KKR, **Forstmann Little** and **Texas Pacific Group** focused on transactions that "kept getting bigger and bigger," Fox says he saw an opportunity for a smaller fund to capitalize on deals that were getting passed up.

Also, as the groups raised larger funds, hired more people and spent more money, they began to have less of a personal impact on the companies within their portfolios, Fox says, and that bothered him.

"With too many people involved, there are too many opportunities for mistakes," he says. "A buyout group has to be small to give companies the kind of attention they need. Otherwise, important things get lost in the woodworks."

Fortunately for Fox, he was not alone in his thinking. He had kept in touch personally and professionally with Dexter Paine, whom he had met while Paine was with **Bankers Trust**. In fact, Paine had arranged financing for the Motel 6 deal.

Paine had since joined **Kohlberg & Co.**, where he stayed until 1997 – the year he and Fox combined their buyout firm ideals and founded Fox Paine, which is based on their common views about "keeping it small."

Consequently, Fox Paine closed its debut fund, **Fox Paine Capital Fund**, in April 1998 on $500 million. The fund was completely invested in seven companies by October 1999. The Foster City, Calif.-based firm currently is in the process of raising Fund II, with a $750 million target.

"The idea for Fox Paine was to take the tremendous experience and expertise that we had developed while working with large companies and focus on mid-cap companies where others with our experience and relationships were not focused," Fox says.

But he makes it completely clear that size is not all that matters — it's the smaller "complicated situations" that appeal to Fox Paine the most – transactions where the deal, the company or the financibility is difficult to orchestrate.

The Road Less Traveled

Fox sites two of the firms' Fund I deals in particular, saying they are good examples of Fox Paine pulling through in tough situations, most notably, when the high yield market seemed non-existent, causing many deals to choke and die.

Last summer the firm ventured into the medical equipment business with the $600 million acquisition of publicly traded **Maxxim Medical** and its former subsidiary **Circon Corp.**, which was then valued at approximately $230 million.

Fox says he and Paine sensed the problem they would have finding high yield financing – considering that many LBO deals died or had to be financially restructured because of the high yield situation – so they instead put together their own group of investors to buy all the high yield debt for the two deals, in effect, financing both transactions themselves "without any help from Wall Street."

"We sensed that the world was changing and rather than just going along on our merry way," Fox says. "We got the deal done any way we could for the benefit of our fund. "

High Hopes

Fox sums up his firm's philosophy with a quote from Sir Nathan Rothschild, the 19th century British banker credited with saving the London stock exchange from collapse by buying up all the shares sold by frightened investors when he was informed by carrier pigeon of the allied victory at Waterloo. The quote reads, "Great fortunes are made when the cannon balls are falling in the harbor, not when the violins are playing in the ballroom."

Relating this to his firm, Fox says, "We try to be somewhat contrarian – to look where there's hair, not necessarily where everything is rosy."

So it is in buyouts that Saul Fox says he will spend the rest of his working years. He's surpassed his own expectations, considering that at age seven he wanted to be an elevator operator, or maybe a clown.

But as a general partner in the world of private equity, life as an elevator operator or a clown might have provided him with more free time. Fox says he goes skiing twice a year, but had trouble naming any hobbies besides interests in art and film. However, he does find time to teach a class on mergers and acquisitions at Stanford and says spending time with his five children definitely qualifies as a hobby.

As for Fox Paine, Fox says the firm is slowly becoming everything he had in mind when he set out on this journey, but is still in the early stages of its formation.

Fox Paine anticipates hiring eight or 10 more professionals in the next two years, he says.

And despite the size of any firm or the reach of its fund, Fox says certain things stick out as the most important aspects of being a smart investor, whether you're a big fish or a small one: comprehensive due diligence, properly structured transactions, hiring the right professionals and treating them, as well as management teams, with respect.

"Things like that make all the difference in the world," he says.

FACT SHEET

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Born: July 13, 1953, Philadelphia, Penn.

Education: B.S., Temple University; J.D., University of Pennsylvania

Career Path: Latham & Watkins 1978-1984; Kohlberg Kravis Roberts & Co. 1984-1997; Fox Paine & Co. 1997-Present

Favorite Book: *Encyclopedias*

Last Book Read: *I will Bear Witness,: A Diary of the Nazi Years, 1933-1941,* by Victor Klemperer

Favorite Movies: *2001: A Space Odyssey* and *Quest for Fire*

Last Movie Seen: the remake of *Richard III*

Favorite Food: Japanese

Favorite Travel Destination: Africa

Number One Pet Peeve: Sloth

Most Admired Historical Figure: George Washington

Favorite Quote: "Great fortunes are made when the cannon balls are falling in the harbor, not when the violins are playing in the ballroom." -- Nathan Rothschild

Investment Philosophy: Buy Low and Sell For More.

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