

## MID-SIZED DEALS HAVE ESCAPED THE DROUGHT

### PRIVATE EQUITY

BY JONATHAN RATNER

The market for highly-leveraged private equity deals involving giant companies like **First Data Corp.** and **TXU Corp.** in the United States, and **Bell Canada Inc.** in Canada, may be tightening up, but that does not appear to be the case in the mid-market just yet.

The space where companies with roughly \$50-million to \$300-million in revenue operate is the focus of institutional fund manager **Penfund**, which is eager to capitalize on any such shift in debt markets — such as yesterday's 50-basis-point cut from the U.S. Federal Reserve.

The firm does equity investing via buyouts and minority investments, and provides private high-yield debt.

"right now, conditions are still pretty good," said Adam Breslin, a partner at Penfund. "There hasn't

been a major bank tightening for the middle market so far."

Syndication desks are having trouble determining the terms needed to make sure their loans find receptive buyers and the banks can get them off their balance sheets, said Richard Bradlow, another partner at the firm. And while the syndication pipeline has frozen up, a huge number of deals still need to make their way through it.

Penfund believes conditions will tighten in the mid-market, but they are unsure when. In Canada, tightening has not occurred because the economy remains stable, Mr. Breslin said. Nonetheless, he expects that any slowdown in the United States will spread to Canada, and that

### 'DEBT IS ALWAYS CHEAPER THAN EQUITY'

will lead to credit issues and tightening.

If the banks tighten and reduce the amount of capital available, demand for some of the alternative debt products Penfund provides will rise, Mr. Breslin predicted. "This has the potential to be a very good thing for our business."

A lot of people are likely waiting on the sidelines to see whether this is going to happen, when,

and how severe it will be. What is for sure is that the turmoil in credit markets means there is less opportunity to generate returns from paying down debt.

"Debt is always cheaper than equity, so the more debt you can employ in the mix, the lower the cost of capital and the more the business is generally worth," Mr. Bradlow said.

Buying companies and loading them up with debt has made a lot of people a lot of money in the past few years. And while credits are still sound for the most part — at least until more weak economic data comes out of the United States, or even perhaps Canada — private equity buyers are no doubt cooling off.

Thanks to a lot of low-cost debt, private-equity groups took hold of the advantage that strategic buyers traditionally had when bidding for companies. This primarily came in the form of synergies and other cost savings.

But if market conditions change, that pendulum might again swing away from private equity and deals that were doable six months ago may no longer be.

Fund managers are keeping a close eye on the current state of debt markets for just this reason. Penfund, for example, points out that although nothing may fundamentally change for a business they are considering buying, changes in the debt market could mean they risk overpaying by as much as 15% to 20%.

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