# Business Better (Season 3, Episode 17): Investing in Consumer Brands – A Conversation with SBJ Capital

Speakers: Jeff Fickes and Porter Hall

Steve Burkhart:
Welcome to Business Better, a podcast designed to help businesses navigate the new normal. I'm your host, Steve Burkhart. After a long career at global consumer products company BIC – where I served as Vice President of Administration, General Counsel, and Secretary – I'm now Special Counsel in the Litigation Department at Ballard Spahr, a law firm with clients across industries and throughout the country.

In today's episode, we're joined by Jonathan Saltzman, Managing Partner at Torque Capital Group; a private equity firm that invests in lower middle market manufacturing firms. Torque brings decades of experience is sourcing, executing, and managing transactions, going beyond only financing companies in order to provide operational and strategic resources. Leading this discussion is my Ballard Spahr colleague, Jeffrey Fickes, Co-Leader of the Private Equity Group. So now let's turn the conversation over to Jeff.

Jeff Fickes:

Well, thank you. This is Jeff, and Porter, thank you so much for taking the time today. We really appreciate you being our guest.

Porter Hall:

No problem, Jeff. Excited to be here.

Jeff Fickes:

I guess we'll get started off with the fact that I'd love to learn and our audience would love to learn about you, your background, and your role with SBJ Capital. So do you mind telling us about that?

Porter Hall:

Yeah, no problem. I joined SBJ back in 2014. I was actually the first non-partner, so it's been a lot of fun. I joke, I think the first thing I did for SBJ was pick out the printer, so I've truly sort of seen things soup to nuts for the company and that's been really fun to see what we've accomplished and what the business has now grown to through our second fund and having eyes on the third fund here.

I'm now a principal with SBJ. I lead our deal execution, portfolio management, and a little bit of deal origination as my colleague Matt Cole, who heads business development, would love to see me maybe out on the road a little bit more and I'll try to continue to do that more as we continue forward.

Jeff Fickes:

How did you find your way into private equity? Tell me a little bit about your professional background.

Porter Hall:

Yeah, I started my career at JP Morgan out of undergrad for about five years and headed back to business school. I went out to Berkeley and I think anyone that goes to the Bay Area, this is ten or more years ago, has a viewpoint that they've got to get into startups and venture capital. And I poked around that for a little bit and ultimately, I decided I didn't have a ton to offer a startup founder. I hadn't started a business, I wasn't an engineer. And I got introduced to lower middle market private equity and that was an area where I thought, hey, the problems that business that is scaling are facing, alignment of incentives, management of capital, return on investment on your capital, those are all problems I'd spent a long time thinking about and working on. And at JP Morgan, I had mostly spent my time focused on the lower middle market businesses, so I was super excited about that sector in particular.

And yeah, the larger cap stuff I think is interesting, but I just find those businesses obviously much more complex organizations and harder to effectuate change. And I thought the Goldilocks between venture and large buyout is where we sit in lower middle market, middle market investment where I thought my experiences were particularly valuable to a seller in a unique way beyond just capital. And further, I felt like we could effectuate change at a pace that is much more difficult in a large cap investment strategy.

So I was sold. I think I drank the Kool-Aid from the beginning. I've been in it now for more than 10 years and I think it's amazing to hear the stories of the founders that we meet with. I have a lot of respect for them. I certainly wouldn't have been able to do it myself and so it's pretty fun and a pretty cool job from my perspective.

Jeff Fickes:

It is amazing. I hear this story all the time of what you just said about why you find yourself in the middle market, lower middle market and the difference you can make is such a consistent theme as compared to startup, emerging companies, and large companies. I love hearing that story. I likewise feel the same way.

Why don't we turn now and talk a little bit about the formation of SBJ, its founding partners, how it came to be, and a little bit about what it is today?

Porter Hall:

SBJ hearkens back to a couple of other funds that our partners were with. Our partners have focused on lower middle market investing for decades now, and wanted to get together after having worked together in some time to do this in a more focused way. So SBJ was founded back in I guess 2013ish, and really partnering with founders is the core DNA of our business. It's, as I said, been the focus of our team for decades and I think it just gives us a slightly different bedside manner, if you will, than some of the other brethren in the industry.

I think most importantly, we view all of our interactions as a non-zero game, if you will. So we strive to put ourselves in the position of our partner companies, in their shoes, understanding what it would be like to go through those processes and try to think about all of this from a perspective of how can we approach this in a way where we all win together?

I think one thing we're very proud of is we've helped more than four companies grow from less than $5 million EBITDA into $500 million brands, and we understand there's going to be growing pains along the way and those things are normal and we should embrace them, the challenge of it, and fix them together.

So we have developed a bunch of resources to help people through that. And honestly, we just harken back on a lot of pattern recognition and experiences. As we like to say, we're not smarter than anyone else, we've just done it a lot more times. And like anything else, if you do it enough, you start to recognize the places that can trip you up and the places where there's opportunities. And we like to think that we are able to lean on those to bring those mistakes that we've made in the past to our founder partner companies so they don't have to burn their hand on the teapot and they can just learn from the scars that we might have.

That's our whole approach. We've been involved with some really great brands prior to SBJ and at SBJ, Peet's Coffee and Tea, J. Crew, Design Within Reach, a host of them, and then certainly within the portfolio, a ton that we're very proud of. So it's the type of environment that I'm drawn to. It's why I joined SBJ is this approach of trying to truly deliver value to our partners beyond just the capital.

Jeff Fickes:

Well, tell me a little bit about SBJ's investment thesis, your focus and whatnot.

Porter Hall:

We're consumer investors at our core. We'll dabble in a little bit of healthcare and services, but ultimately, what we think we're best at is businesses that have a direct relationship with their end customer. And sometimes in a service business, that might be a small business that operates a lot more like an individual than a company. Sometimes that might be a patient in healthcare, urgent care, ophthalmology, but we want to be at a place whereby the consumer is making the choice as to what brand they're purchasing, what company they're using. And we think that our experience in the past has been, and as I was speaking to, allows us to be more helpful in value-adding in those situations and structures and I just think we have a better stable of resources to help in that.

We're reasonably flexible on the size of the business. We invest in anything down to maybe $3 million of EBITDA and up to $20. We're spending a lot of our time in the $5 million to $15 million range. That's, I would say, what the sweet spot is for us, and always or almost always first institutional capital. So we love the story of a founder that is excited about the next five years, maybe even more so than they are about the actual transaction itself. So we're very focused on partnering with those type of individuals whereby we would take a control interest in the company but they would maintain a material ownership percentage and be very, very much involved in the business. Ultimately, it's their blood, sweat, and tears that have got the company to that point and so we have certainly appreciation and a focus on wanting them to continue to be involved.

Jeff Fickes:

Wow. Consumer brands and the consumer sector in general is really, really tough and complex. What is it about that sector, whether it's the background of people in the firm that have been successful in it, what is it that you like and where you see where your organization can add value?

Porter Hall:

Yeah. One of the biggest things we focus on is just looking for places where there's evangelistic-like consumer bases, and be that Troy Lee Designs that we were an investor in, Under Canvas that we were an investor in, Rishi Tea, which we're an investor in, all of these are places where we see there to be a very strong and passionate relationship between the brand and the consumer. And I think we do a particularly good job of scaling a business while understanding how important that initial relationship is to the business and not losing sight on what has made the company special and has helped it get to where it is today. And that's a big focus of ours.

We have a host of resources to make sure we understand the consumer, to understand the brand messaging, to make sure we deliver that brand messaging in a thoughtful way, whether that be opening doors and distribution or customer relationships or recruiting board members to help with that, we have a war chest, if you will, of resources to help those brands.

But we think that is particularly a place, where I think consumer investors have had trouble in the past, is where they get a little bit more into a commodity-like product or lose sight on what made the business special to begin with. And so that's been a very successful approach to us and we like to be within businesses that are leaders in the niche that they're operating in. That doesn't necessarily mean they're the biggest brand in the entire industry. Take Rishi Tea, for example. That is an amazing specialty tea manufacturer. I personally think it's the best tea on the market. Is it as large as Lipton? Of course not. But in the areas that it competes, it is the stalwart of that industry and I think that makes it very special and provides us a lot of opportunities to help the business grow from there.

That is what we really look for as we enter into consumer companies is a very unique relationship with the end consumer.

Jeff Fickes:

If you don't mind, talk a little bit about the resources. You've mentioned a few times about bringing more than just the capital and the resources you provide in this sector. Can you give me some examples as to how you've helped your resources and your thought leadership have helped fuel the growth and the enterprise value of the companies in which you invest?

Porter Hall:

Yeah, of course. The reality is, and probably some of my colleagues would be on me, but capital's a commodity in the end of the day. It all spends the same and there there's no way to differentiate on capital alone. And so what we want is a situation whereby our prior partners and CEOs say, "The SBJ guys pulled their weight and more so in delivering value to the business and didn't just rely on the team to execute that."

We've hired an internal head of talent who's an amazing individual and able to help us recruit new positions. We partner with an outside group to recruit specific outside board members for each of our portfolio companies. I think an old approach has been to rely on friends of the fund, if you will, and look, I think it's sort of an open question whether or not there's alignment of interest there. And I think our approach of saying, "Exactly who do you need? And we'll go out and find that person and recruit them to the board" is really powerful.

We have a strategic partnership with an operations group that helps with all reporting, IT systems, all of these things as a business scales that, a lot of times, maybe a founder family-owned business hasn't had to think about as much, particularly if they haven't had that on the business and haven't tried to scale as rapidly as we're all trying to do post-our investment. That puts a lot of pressure on it. And so to have a group that we can have come in for the first three months and be a crew that helps to get the business on the right systems reporting the right way in a rapid fashion without taking time out of the team who's got to run the business day to day, that's all really powerful.

Those are some of the key ones. Of course we have a host of relationships with consumer research companies, with site-based analysis companies, with branding and marketing firms that we pull in on a little bit more of a bespoke basis. And all of those, I think as I was saying, because this is the only thing we do and because we're only investing in partner founder-owned businesses, we get to do this every single time. And so as another fund that might have to pull this resource in or every other, every third deal, we build a much deeper relationship with these groups and I think it shows in the value they deliver to the companies, and honestly just the love we get as opposed to maybe how they allocate their time to other groups.

Jeff Fickes:

With respect to growth, how does M&A play a role in that, if it does it all, versus trying to expand the product offering, the consumer product offering, or add new locations, a more organic nature of growth?

Porter Hall:

We approach each of the investments on a standalone basis, so we would never say the strategy for one should carry over to the other. And some brands lend themselves to the acquisitions. We own an ophthalmology group down in Tampa-St. Petersburg. We've completed multiple acquisitions since that has closed and I think we'll complete more before that deal is exited and that's the right approach to that business.

In other brands that we've been in, Swensons our restaurant chain, it's been a focus on expanding into new geographies outside of Akron, into Cleveland and down into Columbus and Cincinnati, and hopefully further from there. I think we like to sit down upfront in the beginning, and more important than should we grow via acquisition or de novo is having alignment with the team on how to grow. Both of those strategies I think are very powerful. We've executed them both successfully, but where there are problems is where there's a misalignment on what the team thinks is the right approach and what we think is the right approach.

So we focus very much on upfront sitting down and making sure that team's part of that process and saying, "Hey, here's where we think we should aim to achieve. How all do you think about getting there and what do you think is the right approach to doing that?"

So yeah, I would say most of our investments should work without acquisitions and acquisitions are a little bit of frosting on the cake, but there are occasions when they're really good frosting and we focus on them a touch more than others. But yeah, like everything else, we try to tailor our approach to each of the investments and not push a strategy on the team.

Jeff Fickes:

How do you work with the founders who continue on with the business and have a material portion of continued ownership? Some of them are really good, founders are sometimes really good at running the existing business. They're in the day-to-day operations, and now as part of it, and they're very eager to grow the business and they love having you as a partner, but they need some education, they need some mentorship. They may even need collaboration with CEOs or founders of some of your other portfolio companies so that they learn how to work on their business instead of in their business on a day-to-day basis.

Porter Hall:

It's a great question because I think one of the hardest things a founder has to go through is the process from which they were the owner of everything to a delegator and reliance on other people. And we look for that upfront a lot. I would say the best leaders surround themselves with a better team and the leaders that have struggled typically are nervous to add better teammates around them because they're concerned on how that might make them look. And so we do spend a lot of time upfront trying to understand the motivations of our founders. We look for people that are good listeners, that are intellectually curious, that are open to new ideas, and that's ultimately what we strive to be.

Importantly, we will, as we've mentioned, bring in outside board executives so that they have a mentor that's done this before as a sounding board to work through this with them, understand the process that they're having to go through, and honestly just be someone to talk the ideas through that isn't SBJ or isn't the team. We've invested in career coaching and executive coaching where we think it's important and logical, and certainly we'll recruit in, help the invest individual recruit in new executives that can help them bring in a caliber of individuals that they feel more comfortable delegating to. But that's a shared problem. It's not the founder's item to figure out. It's something that we all need to do together.

And one of the biggest things for us, is just we're sort of maniacal around being aligned on incentives because I do think that's a big impact here on how people act and perform. And so we try to avoid complicated structures. We like to be in the exact same security heads-up with our founders. We try to avoid contingent payouts and such because we think if people are aligned on incentives, we all at least have a shared vision and goal then, and it's easier to work through the inevitable growing pains that are going to occur. And I think we try to sit down upfront and say, "Hey, the most important thing we can all do is just have honest and open communication and conversations. There are going to be things or changes that we all need to work through together. And change isn't always easy, but hopefully it's all for the better and it creates a bunch of opportunity."

And usually, I would say once that momentum starts to pick up, that individual usually very much embraces the new environment, sees the advantages of it, and gets super excited about their team achieving things as much as themselves achieving things. And over time, sometimes the founders come to a point where they say, "Yeah, I've loved it. I want to continue to be involved, but I want to be more in an advisory role," and that's totally fine. We will work through that transition with that individual when that time comes and make sure we find the right steward of the brand going forward. And that's something that is a normal process of any business's maturation, but usually that's a collaborative conversation and decision.

Jeff Fickes:

That's fantastic. Well, my knowledge about your organization is that you actually spend a lot of time in person with your founders and your management team. Is that part of your strategy to have basically strong personal relationships to help align the incentives? Some private equity investors might be more hands off, but also don't spend time on site, don't spend time in person with the founders and the management teams.

Porter Hall:

Yeah, I think it's critical, particularly as we've exited a pandemic area where I think people have leaned into, appropriately so in many instances, more video calls and such. There's still something particularly early on in this process that's very special about being together in person. We like to say, "Hey, the crazy thing for a founder is they're going to go marry somebody and they only get to meet them once or twice often." That's a really hard situation and we always think it's a little odd honestly for that individual to have to make the decision with that, so anything we can do to be down in person.

The most recent deal we closed, which we'll announce soon, actually I think a big part of winning it was we flew back down just to have dinner one last time. I think the founder was pretty surprised that, it was across the country that we went, we flew five hours just to grab dinner and get back on a plane and go home. But if you're going to be in business with somebody, you should expect someone to give you that level of attention and support. And if they're not, I think it's an open question as to whether or not they're the right partner. At least that would be how I would think about things.

And so we always do the board meetings down in person at the business. We don't ever make people fly back out to us. We try to get down on other occasions. We make sure we bring the broader team into events, try to do team-building things, whether it be a little event at Topgolf or at a baseball game. It's important to understand that the reason our businesses are successful are certainly not because of us and not just because of the executive team, but because of all the people that work in that company. And I think embracing that and making sure that we have those relationships and open communication is really important because when there needs to be things worked through, if you can rely on those relationships, we found it to be a much better outcome.

Jeff Fickes:

That is so true. You've given me some great examples so far of the way you bring additional resources and thought leadership and experience in networks to bear. Tell me a little bit about a few examples where you or other people within your network have helped the founder after the transaction implement, come up with a new concept idea, not just adding new sites with the same thing, but they've got these evangelical followings for their existing products or services where you saw strategies or complimentary products or services that could be accretive to the organization and were then implemented strategically and helped immensely grow the value of the company.

Porter Hall:

Yeah. I think one where this is happening real time is at our... We have an investment in Rishi Tea & Botanicals that I've mentioned, and we have a great board there, former Illy president and CEO, and an individual out of Conagra. And that group has gelled and come together in a way that is just really fun to watch. And the way that they have helped the company think about investing in marketing and advertising and different channels to help grow the underlying business has been really compelling.

So just to give an example, one of the big things we think about is how do we think about... We view that if we can get Rishi in your cup, we'll convert you. I'm confident that if you drink Rishi Tea, you'll be a convert if you like tea. And so one of the big things we've focused on is how do we think about expanding distribution in a way that achieves that? And maybe that's not always the highest margin channel and maybe it's not always as valuable, directly to the bottom line, as maybe the D2C channel or an e-commerce channel, but getting the individual into that ecosphere and then letting them matriculate from a tryer into the evangelical group is extremely powerful.

And so to change the viewpoint on channel strategy to drive a little bit of a marketing viewpoint has been one that is different than the company had historically thought about it, and honestly it's different than most businesses think about it. I would say tea is a somewhat unique experiential brand or experiential product I should say, that lends itself to that approach. And I think that's a place where we're super excited to see how things play out. We're a little less than a year into that one, but the momentum has been fantastic and I think that team's got a lot of big things to achieve here in the coming years.

Jeff Fickes:

That's great. What is your investment horizon and can you give me a few examples of some "home-run exits" that you've been able to achieve?

Porter Hall:

Yeah. In general, we go into our investments thinking that we'll be five-year partners. There's nothing sacrosanct about that specific timeline. Sometimes it's a touch quicker and sometimes it's a touch longer. But ultimately, our whole focus in the beginning is how do we build a good business over time? And whether that takes four years or six years is irrelevant, but what we don't want to do is say, "We're going to sell in three years to this person" because that is inevitably where I think people have gotten in trouble historically, which is being too focused on one specific approach and thinking that's all your eggs in one basket, if you will.

And so I think that strategy, particularly as we've worked through the pandemic and a turmoil in the credit markets and the banking markets, has been really powerful because the reality is some of the groups that we thought would be buyers to businesses weren't there at the end when we got to sale because they had their own issues or there was a credit market issue. It's really hard to know.

So we are really proud of the exits we've had. Under Canvas is now owned by KSL Partners, which is massive entertainment private equity firm out of Denver. That was a great investment for us. Troy Lee Designs is now owned by a European private equity-backed business that we were still really excited about. When we first got involved in Troy Lee, the inventory was all in container trucks in the backyard. And now that business has grown exponentially and obviously has a sophisticated 3PL. And to see where it is today versus where we got it, and yeah, sure, obviously the economic return is exciting, but the real fun of it is just to see what you've built and the byproduct of that is really the economic outcome.

We aren't focused as much specifically on that. Our viewpoint is always, hey, grow a business and build a good business and everything else will work out just fine.

Jeff Fickes:

Is there anything else that you'd like the audience to know about SBJ and its strategies or future strategies or successes?

Porter Hall:

One of our biggest things is we're transparent and open. So one of the things we always say is, "If you partner with us, we'll give you our Rolodex. You can call anyone you want, you can ask them any questions you want." I think you'll find out, yeah, I think we're confident that you're going to get good answers, that we're fair and good listeners and responsive and driven and hopefully just fun to work with, which honestly, it does matter when you've got a partner that you're going to be spending a lot of time with. And so yeah, that's an important part of our strategy and our approach here.

And yeah, I think the other thing I guess to mention as to what is sort of on the horizon for us, what we want to be is a one-stop shop, if you will, for family founder-owned businesses. And so we're working on a fund strategy that would allow us to facilitate a minority investment, would allow us to facilitate a debt investment on top of the control buyout group that we currently operate. And so I think a little preview of what the future might hold is a model whereby if you would like capital to support growth, if you'd like capital to diversify your own wealth or if you're just looking to sell, if you're a founder or entrepreneur, SBJ will be the right home for you and that's what we're trying to build longer term.

Keep an eye out for some announcements to come down the road.

Jeff Fickes:

Yeah. More to follow of course, right?

Porter Hall:

Yes. Right, exactly.

Jeff Fickes:

Well, Porter, thank you so much for your time. We really sincerely appreciate it.

Porter Hall:

Yeah, thank you and appreciate the time. Obviously it's a pleasure to partner with you all, always, and I look forward to continuing to do so down the road.

Jeff Fickes:

Thank you.

Steve Burkhart:

Thanks again to Jeff Fickes and Porter Hall. Make sure to visit our website, www.ballardspahr.com where you can find the latest news and guidance from our attorneys. Subscribe to the show in Apple Podcasts, Google Play, Spotify, or your favorite podcast platform. If you have any questions or suggestions for the show, please email podcast@ballardspahr.com. Stay tuned for a new episode coming soon. Thank you for listening.