

Peter Hermann

Adventure capitalist

Heritage's Hermann took the less traveled road in buying and selling family businesses

BY CRAIG M. DOUGLAS
JOURNAL STAFF

To crystallize the risks and rewards of investing in family-owned businesses, Peter Hermann reaches back to a meeting about a prospective deal several years ago involving two brothers, a pistol and a whole lot of bad blood.

Those three factors collided early on, well before Hermann's private equity firm, **Heritage Partners**, would invest millions of dollars for a stake in the brothers' company.

"Someone pulled a gun. I think it was one of the brothers. Or maybe it was one of their wives. I've forgotten," said the 52-year-old Hermann. "We had to call a time-out."

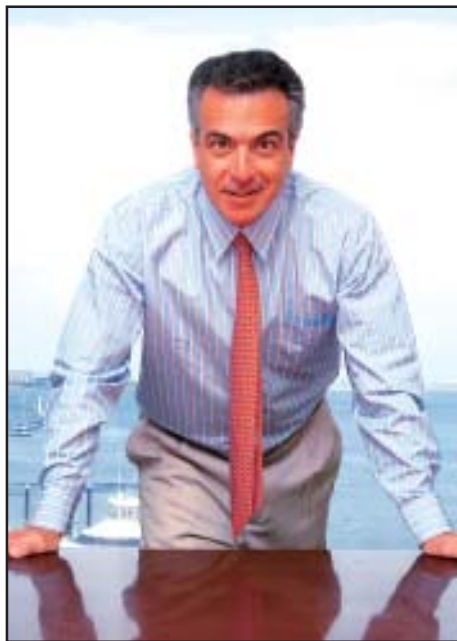
He calmly noted that the showdown was just one of the many bizarre situations he has encountered as a buyout specialist over the years.

For a guy who once sought the so-called romantic life ("writing a book, raising sheep ... whatever those people do"), Hermann took the long road to becoming a respected player in Boston's private equity community. Some would say he's all the better for it.

His success has come in a sector dominated by well-heeled, Ivy League-educated principals who gravitate toward the mind-set that bigger is always better. On both fronts, Hermann stands out, partly because of his nontraditional career path, but mainly because of his appetite for the small, messy deal.

The second of five kids growing up in Newton, Hermann traveled abroad as a teen with his father, then a college professor, and ultimately enrolled as a British history major at the University of Sussex in England. With an eye toward political revolution, his attention shifted from Oliver Cromwell and the British civil wars to the upheaval taking place in Portugal during the 1970s.

Hermann would spend a year in Portugal, studying the socialist movement under way, before receiving a government letter ordering him to either leave or cease his poking and prodding. Hermann obliged, promptly enrolling in a fledgling graduate program in finance



SANDIE MCDADE-ALLEN

FROM THE FILE

Position: General partner, Heritage Partners

Age: 52

Education: Bachelor's in 17th century British history, University of Sussex, England; M. Phil in economics and business, Oxford University

Quote: "Life is short. The goal is not to be managing General Motors. What's fun is investing in family-owned businesses."

and economics at Oxford University.

In retrospect, Hermann says those experiences — along with a brief stint as a U.S. State Department aide in Portuguese-speaking Guinea Bissau, Africa — were key to his eventual segue into private equity, an industry with its own fair share of upheaval and hostile takeovers. For him, the parallels were obvious, in terms of the role that outside activists can play in reshaping an organization.

"The complexity," he said, "is dealing with human beings with huge egos."

He eventually was recruited by Bank of Boston, now part of Bank of America Corp. (NYSE: BAC), to work as a commercial lender in its Africa and Middle East division, and was rescued after about a year in Cameroon by Michel Reichert, a friend and colleague who was running Bank of Boston's acquisition-finance group.

At the height of the 1980s buyout frenzy, the duo quickly determined that "all of the action" was flowing toward the day's largest private equity

firms. By 1986, they convinced Bank of Boston CEO Chad Gifford to let them roll the dice as private equity investors. "He said, 'See what you can do,'" Hermann said. "We were a couple of guys trying to figure out how to do this with no budget at all."

What ensued was a quixotic, cross country fact-gathering mission that saw Hermann and Reichert interview hundreds of business owners. The duo would eventually parlay their findings into a business plan promoting "The Private IPO" — a funding option for family businesses that allows owners to enjoy some liquidity while retaining roles in their companies.

Most private equity firms tend to buy a majority, if not all, of a company's stock. Once in control, senior management changes are commonplace. Hermann says both trends are a nightmare for most family-owned firms, especially those passed down through multiple generations.

Hermann et al spun off from Bank of Boston in 1994, raising Heritage Partners' inaugural \$150 million fund. That partnership generated an 83 percent internal rate of return, Hermann says, and led to two follow-on funds in 1997 (\$380 million) and 1999 (\$850 million).

As in the case of the gun-wielding brothers, Hermann has proven adept at navigating family dynamics and getting everyone pointed in the right direction. Among the company's recent wins was June's sale of Castle Rock Industries Inc., a maker of cleaning equipment and supplies, which generated a 350 percent return on Heritage's initial \$25 million investment. Another big win came last October when Heritage cashed out on an investment in Skilled Healthcare Group Inc., a provider of elderly-care services that was acquired for \$640 million.

Sandy Francis, the former vice chairman of Castle Rock Industries, said several things stood out when dealing with Heritage, namely its intent to do right by the company's owners. He pointed to one example that saw Hermann chip in an extra \$9 million to the Francis family after the business was sold, a payment that was based solely on a word-of-mouth agreement early in the investment process. Said Francis, "Our lawyers thought there was no way we'd ever see that money. Peter did what he said."

Looking back, Hermann regrets having raised such a large fund in 1999 — at the peak of the last economic cycle — noting the lure of loose money outstripped the firm's original mission: Investing in and growing family-owned businesses.

He expects the firm's next fund, due sometime next year, will likely total between \$200 million and \$400 million. "Life is short. The goal is not to be managing General Motors. What's fun is investing in family-owned businesses," he said.

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