Meet The Manager

Steven Klinsky, New Mountain Capital

Steven Klinsky, founder and chief executive officer of New Mountain Capital, knows a few things about the private equity industry. The former senior partner at Forstmann Little has been investing in private companies for more than 20 years. In January 2000, Klinsky left Forstmann Little to strike out on his own, forming New Mountain Capital with Robert Grusky and J. David Wargo. The firm recently closed its debut fund on $770 million, well above its initial target of $600 million. Fund raising for this first-time vehicle was no doubt aided by a strategic investment in New Mountain made by the California Public Employees' Retirement System. To date, New Mountain has done one major deal – a $115 million investment in publicly traded education company Strayer Education Inc. Klinsky recently spoke with PrivateEquityCentral.net about his new firm, its new fund, the post-secondary education sector, and the appeal of the middle-market.

PrivateEquityCentral.net: You just closed your debut fund on $770 million, $170 million above the original target. It's a tough fundraising environment and this is a first-time fund. What about your investment strategy do you think investors found appealing?

Steven Klinsky: I think what they liked about New Mountain was the track record of the principals. I think they liked the fact that they could have worked at any size firm that they wanted, but decided to focus on the middle market, where the opportunities for returns are stronger. And I think investors liked the fact that we're focused on growth and value added to the company and proactive deal search.

PEC: Your firm's first and sole investment was in Strayer Education. What about that company attracted you and what do you think its prospects are?

SK: First of all, we had identified Strayer's industry before we found Strayer. We like the post-secondary education industry. It's one that has strong secular growth. It actually does better in a recession and has high barriers to entry, high operating margins, and so forth. We think it's an excellent industry.

Strayer was a particularly interesting company in that industry because it has the highest margins of any of the publicly traded companies. It has 40% operating margins. It's had about 20% top-line growth for the last 10 or 15 years — exceptional consistency. It was at a very big price-to-earnings discount to other companies in the industry because there wasn't a management succession in place, there wasn't a growth division in place, so New Mountain was able to come in and solve the company's problems, and that's why the stock has gone up so much. We were able to bring some extra value to the company, and that has already led the stock to more than double since we made the investment.

PEC: What is it about the education sector that leads you to believe it will take off?

SK: Seventy-five percent of Americans have never gotten a four-year college degree, and the wage gap between college-educated workers and non-college educated workers keeps growing and growing. So, basically, a student can go to a school making $20,000 before they go to school and end up making $50,000 once they graduate. It's a very high return for the student, and there's a huge unmet need. It's grown very, very well even in good times, and when unemployment goes up, more workers go back to become educated and get their careers started again.

PEC: Will the fund be looking at undervalued or distressed deals at all, or are you going to focus on growth industries?

SK: Well, we're looking for businesses that we think can become very important businesses in very important industries. Strayer was an undervalued situation because there were issues that held the stock down. What you can do as a private equity investor is actually add value to the company, and you don't have to sit there passively. We will look at undervalued situations, we will look at distressed situations, if we believe that, fundamentally, there's a franchise there that can be a growing, important business.

PEC: What was your role at Forstmann Little, and what did you learn there that has helped you at New Mountain?

SK: My own background is that I was co-founder of Goldman Sachs' leveraged buyout group in the very early 80s. In 1984, I joined Forstmann Little as their fifth professional. It was a $200 million fund. I was a full partner by 1986, and then by the early '90s, I had become the most senior partner of the firm other than the two Forstmann brothers. That's what I did until 1999, when I went off to start New Mountain. We had a tremendous track record there. I think we made $6 billion in gains throughout the '90s — a very strong, consistent record. It was a great firm in the years that I was there, and we're trying to continue that spirit on at New Mountain. We just think the middle market has more opportunities for exceptional returns these days than the mega-market.

PEC: Is that one of the reasons why you left Forstmann Little?

SK: I think in the middle market, you can be much more of a craftsman because you have less money to put out. It's also just a terrific position to be a manager at your own firm.

PEC: Do you plan on raising any other types of funds at New Mountain?

SK: We're not trying to become a fund family. We invested very heavily into this fund ourselves and are very focused on earning excellent returns for this fund. I didn't come in here to try and create a supermarket of funds. We're just going to try and do a great job with this fund.

PEC: How did your relationship with CalPERS come about, and what are the advantages of that relationship?

SK: CalPERS is a very important limited partner. As I was just starting to form the idea of this firm, I got together with CalPERS, they have an organization called Grove

Street that is a gatekeeper for them that tries to find the best funds for CalPERS to invest in, and the principals at Grove Street have known my track record when I was at Forstmann Little, and so when I was setting up on my own, they brought in CalPERS, and CalPERS made a significant investment right off the bat and helped us get started in the first fund.

PEC: What kind of changes do you see on the horizon of the private equity industry?

SK: I think you may see other examples similar to New Mountain, where people who have very strong track records at mega-funds go off and create their own new generation of leaders. You'll see some more of that as time goes on. But private equity is always a great opportunity, but it's not a situation where everyone does it one way, or everybody does it the other way. It's a case-by-case basis of trying to add value to the investments that you make.

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