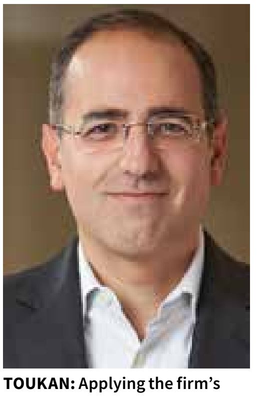
SK Capital moves to the middle

Catalyst fund will focus on family-owned businesses and smaller carve-outs

Vincent Valk

Private-equity firm SK Capital Partners (New York, New York) earlier this year raised a $415-million fund to focus on smaller, middle-market chemicals and materials investments. The fund, called Catalyst, will have a particular focus on corporate carve-outs of a smaller size than SK Capital's usual transactions, and on family- or founder-owned businesses. The first two acquisitions under the fund, engineered compounds maker Techmer PM (Clinton, Tennessee) and the specialty polymers business of oilfield services firm Baker Hughes, were announced in late July.


TOUKAN: Applying the firm's playbook to smaller deals.

The fund will follow SK Capital's playbook in terms of "the type of investing and being solely focused on chemicals, materials and pharmaceuticals," says Mario Toukan, managing director at SK Capital. The firm is often a longer-term investor than most private-equity investors, and tends to focus on opportunities for operational improvements and growth investing. "We formed the fund in order to continue building on the firm's history of investing capital and deploying the SK Capital playbook in the lower middle market," Toukan says. "We are one firm, with two funds applying a consistent process and philosophy across the entire spectrum of deal sizes."

The fund "has access to all the resources of the firm, including the brand, relationships, intellectual capital, and processes that SK Capital brings to the table," Toukan says. However, the fund has its own dedicated investment team, including Toukan, managing director Jon Borrell, vice president Dan Lory, and operating partner and former KMG Chemicals CEO Chris Fraser. "The expansion of the SK Capital team to support SK Catalyst was made easier because we've all worked together in different capacities over the years," according to Toukan.

Right-sized fund

SK Capital's flagship fund was closed in early 2019 with $2.1 billion in capital, some of which has already been deployed. The fund is the largest in the firm's history, and by a substantial margin—the previous fund, which closed in 2014, was worth $1 billion. "The firm has historically been 'size agnostic' and that remains true today. However, the dual fund approach represents an evolution toward having on one hand greater amounts of capital at-the-ready for larger transactions, while on the other hand offering an appropriately sized vehicle to construct a concentrated lower middle market portfolio," Toukan says.

Pursuing smaller and middle-market deals with the flagship fund is possible in theory, but in practice presents some challenges that a separate fund solves. "From an allocation of resources standpoint, smaller deals often won't move the needle as much in a larger fund," says SK Capital managing director Jon Borell. "And the way we approach the market is to have a more concentrated portfolio. We put significant time, resources and focus into transactions and driving improvement in our portfolio companies. It's hard to have dozens of investments in a fund and apply a consistent amount of attention and resources. So it was important for us to have a separate fund that we could create a team around and dedicate the recourses necessary to be transformational investors."

The investor base for the Catalyst fund is similar to that for SK Capital's flagship fund, although some investors who fell away as the fund size increased have come back for the new fund. The fund also gives investors access to growth potential in smaller businesses.

Deal types

Corporate carve-outs and privately-held businesses, very often owned by families or founders, will be the most logical investment targets for the new fund, according to Toukan and Borrell. Carve-outs, of course, can be any size, and SK Capital has done larger carve-outs with capital from the flagship fund, such as plastics compounder Geon Performance Solutions, formerly a division of PolyOne (now Avient). But carve-outs can be smaller, too. This can even include carve-outs form large companies, including those resulting from the spate of megadeals a few years ago—large companies often shed quite small businesses, and these transactions can be especially complex.

Private family- or founder-owned businesses will be another focus for the fund. These types of businesses tend to be smaller, and private-equity firms with a lower-middle-market focus frequently invest in them. For SK Capital, "many of our deals will involve a family or entrepreneur who is looking for a partner to support the next phase of growth and improvement of the business," Toukan says.

The two transactions that the fund closed in July—its first two deals—are clear examples of each archetype. Baker Hughes's specialty polymers business is a producer of low-molecular-weight polyolefins, with manufacturing operations at Barnsdall, Oklahoma. "It was a complex, messy carve-out and our expertise, both in the industry and in carve-out transactions, gave the seller a lot of certainty," Toukan says. The deal is expected to close in the second half of this year.

Techmer PM, a maker of engineered compounds and polymer modifiers, was owned by founder and CEO John Manuck prior to being acquired by SK Capital. Manuck retains a stake in the company. The deal will allow Techmer to grow beyond North America. "What we see is demand among the global OEMs for a reliable, high-quality, innovative partner, and we find it necessary to have a presence on every continent," according to Manuck.

Both transactions were in process as the COVID-19 pandemic hit, which underscored the importance of SK Capital's relationships in industry. "Our DNA is about building strong relationships ... obviously that's been even more critical during COVID[-19] because these deals tend not to happen without them," Toukan says. Both companies performed strongly during the peak of the pandemic in the second quarter, he adds. ■