

Neal Aronson's vision for Roark Capital Group runs counter to prevailing private equity trends, and now, while other firms falter, Roark is reaping the rewards. Here's why.

Sunny and clear

The view from Roark Capital's glass tower

By Julie Bennett

The news from the outside world was stormy. Large private equity firms, including Blackstone in New York and Sun Capital Partners of Boca Raton, were losing money, or in Sun's case, losing portfolio companies to bankruptcy. Franchise consolidator NexCen Brands, of New York, was facing financial peril and Kahala Corp. of Scottsdale, a holding company for 13 franchise brands, was being castigated in the mainstream press for not supporting its franchisees.

But all was sunny on the 25th floor of a glass tower in Atlanta, where Neal Aronson, the founder of Roark Capital Group and two of his partners, Erik Morris and Toby Chambers, sat in a sleek conference room and pointed out the leafy neighborhoods where they now live. Aronson's vision for Roark was to run counter to prevailing private

equity trends, and now, while other firms falter, his firm is reaping the rewards.

Aronson calls himself "the poster child for hope" in a private equity industry that is dominated by a network of males who hold MBAs from Ivy League colleges. Aronson has an undergraduate degree from Lehigh University and prefers to hire people like Morris and Chambers, who also do not have their MBAs. Aronson began his career on Wall Street, first at investment bank Drexel Burnham Lambert, then at two private equity firms, Arcadia (now Oak Hill) and Odyssey, where his job was to find investments in the franchising industry. In 1995, his uncle, Mike Leven, the former president of Holiday Inns, suggested the two of them buy a small franchised hotel company, U.S. Franchise Systems, located in Atlanta.

"The move was easy," Aronson said. "I was single and owned only what would fit into a small Manhattan apartment." The move into franchising was also smooth, and "it gave me a completely different perspective on the people who operate franchises and their attention to detail," Aronson said. He and Leven

grew U.S. Franchise Systems to more than 400 Microtel and Hawthorn Suites hotels, then sold the company in 2000. "Everyone thought I'd move back to New York," Aronson said, "and join one of the big PE firms. I was talking to a mentor, Odyssey co-founder Jack Nash, and he asked what I'd really like to do. I described a hypothetical firm that worked with entrepreneurs who had started small businesses and grown them into larger entities. 'Why don't you have the guts to start a firm like that yourself?' Nash asked."

Aronson did just that. He rented a small office in Atlanta and named his new firm after one of fiction's most famous nonconformists, Howard Roark, the architect hero of Ayn Rand's novel, "The Fountainhead." Aronson raised some money, mostly from investors he'd known in New York, and in 2001 bought controlling interest in Carvel, a franchised soft serve ice cream company in Connecticut, for \$30 million. "The brand had been neglected," Aronson said, "and we spent the next 18 months working with its franchisees."

Unlike most private equity firms that hold a company



Neal Aronson of Roark Capital calls himself "the poster child for hope" in the struggling private equity industry.

for three to five years, then sell it at a profit, Roark still owns Carvel, which it runs through its FOCUS Brands subsidiary, along with other food acquisitions Cinnabon and the international division of Seattle's Best Coffee (2004), Schlotzsky's (2006) and Moe's (2007). Today Roark owns 14 franchised businesses with more than 2,500 franchisees, 13,000 points of distribution in 50 states and 33 countries and \$3.5 billion in annual sales. Other franchises include: Fastsigns International (2003); Money Mailer (2003); McAlister's Deli (2005); Batteries Plus (2007) and Primrose Schools (2008), plus partial ownership in some hotel properties. Non-franchised holdings include Ace Mortgage Funding ("It's not doing too well now," Aronson said) and companies involved in financial services and wood manufacturing.

Roark grew as well, to five

people in 2003 to 31 people now, including seven partners, plus 850 people who run FOCUS Brands from the field and from a trio of low rise office buildings in the northern part of Atlanta.

The firm still has its original investors, Aronson said, plus investments from wealthy families and the endowment funds of large colleges and universities. Unlike traditional PE firms that collect money into a fund, then shop for companies, Aronson launched Roark by calling in investments on a case by case basis. Roark raised its first institutional fund in 2005 and its second fund closed in early 2008. "We have \$500 million invested," Aronson said, "and another billion dollars waiting if I send out a fax asking for money." These investors, he adds, are comfortable with Roark's model of holding companies for the long term.

Roark purchases companies

with less leverage than other private equity companies use, so the firm is less squeezed by current constrictions in the debt markets. And while other private equity firms are trying to shed some of their recent purchases, Roark is seriously shopping. "We evaluate 200 franchise companies a year," said Chambers, "and may buy one or two of them." Those they select must have a unique product, strong managers, like Batteries Plus and McAlister's did, who will take a stake in their companies, and a solid franchisee base. "If you look at franchising as a pure financial vehicle," Aronson said, "it can blow up on you, just like what happened to NexCen."

The problems affecting another PE firm actually helped Roark, Morris said. "Primrose School was for sale in 2006 and Roark participated in the auction, but lost to American Capital of Bethesda, Maryland. When

the credit crisis hit, American Capital decided to return to its core business, which was mezzanine financing, and agreed to sell us Primrose."

Primrose CEO Jo Kirchner, whose office is in nearby Acworth, Georgia, said she's thrilled her franchised network of 189 educational child care centers has landed in the Roark stable. "I'm already picking up some best practices from other Roark CEOs," she said. "And I certainly agree with Neal's goal, to acquire high quality brands and grow them at a controlled pace."

Roark is meeting all the goals he set seven years ago for his non-conformist private equity firm, except for one, Aronson said with a smile. A couple of the women the firm hired recently as vice presidents do have MBAs—from Harvard. ^{FT}

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