Complete Transcript: HALO Talks with Eric Epstein
Posted July 19, 2023

Pete Moore (00:04):

I want to thank all of our listeners for several years of dedicated and loyal listening throughout the Halo Talks 400 podcast completed to date. We're going to a thousand by 2024. If you're so inclined, we'd love to have you go to iTunes for us, fill out a review so we can keep this podcast rolling globally. We are now on Chartable's top lists and moving up the charts. Also, if you want to educate yourself on the new year, please go to the halo academy.com. Take a look at what'll be done with 150 executives in the halo sector to get them smarter, get them prepared for capital raises, and also more winning. Thanks, have a great season. Let's go. This is Pete Moore on Halo Talks NYC. I have the pleasure of having one of my longtime friends in the halo sector join me. We are gonna do a crash course on private equity and growth capital, bringing to you live from San Diego, Eric Epstein, E two Ventures by way of Manhattan Beach, by way of Hawaii, and back to me.

Eric Epstein (01:19):

What up, Peter? Always a pleasure.

Pete Moore (01:21):

Let's just air it out to end up the first day of the trade show. First of all, give everyone a quick background, how long you've been in private equity, putting deals together, and then we're gonna talk about some interesting stories along the way. All right.

Eric Epstein (01:36):

Well, hey, Pete, I appreciate it. We're here down at Ursa, having a good time. San Diego's never been colder. Again, my name's Eric Epstein. I started in private equity in 1993 in New York City. My first job was at the Blackstone Group, believe it or not, 30 years ago. Started, started out there for a couple years. I worked with a couple private credit funds after that, and then I was in the private equity group at Cerberus Capital for 10 years in New York, in, in Los Angeles and California. So I've been doing this for a while. At the moment, I act as an independent sponsor, so I work without a dedicated private equity fund, but I have many relationships with family offices and the institutional capital partners that will partner with me on transactions in which I pursue. And I spend a lot of my time within health, wellness, and fitness, which is why we're here at this. One of my favorite, the Halo favorite trade shows.

Pete Moore (02:27):

The halo. It's called it the Halo Effect. So Eric and I have been friends for at least 15 years now, I'd probably say. And you've been one of the early investors in whether it's bricks and mortar, franchise, franchisor, franchisee, you know, as you look at different business models and you say, Hey, that's interesting. I want to get in on the ground floor, like you're in on the, on the Crunch deal, which I'd say is kind of the ground floor on the franchising side. What are some of the things do you look at and that are important to you? And maybe like if you were to force prioritize, like, I got management, I got ebitda, I got unit economics, or, you know, gimme like a laundry, you know, short, short list of like, if they don't check these boxes, I'm not interested.

Eric Epstein (03:09):

It's a great question. So, so first let me tell you what I don't do, which is people who know me, I'm a health and wellness fanatic, and the first thing I try to do as, as someone who's very passionate, and I think, I guess I'll say on the leading edge of identifying trends, is I wanna make sure that my own personal passions I don't confuse good economics and good transactions with my, my own personal passions. So the first thing I try to do is make they're cloud.

(03:34):

This is make sure that my perspective is actually balanced. Yeah. in moderate and not, not based on some of my extreme passions within the sections. Right? That's actually the first thing I do. But no, on a, on a serious note look, there's, there's, there's different, so many different areas within the Halo. The Halo umbrella, if you will. So look within, you know, I am a Crunch Fitness franchisee in the Northeast, and so I've had an interest in multi-unit for many, many years. As you know, you know, you look at the unit economics and find out where there's opportunities. You know, I pursued a number of planets over the years, early on Uhhuh, you know, kind of well before the private equity consolidation and before valuations went absurd was always kind of cover bid on transactions I pursued in that area, but was very compelled with the H V L P thesis along with those unit economics and, and sought opportunities after planet. And so Crunch was actually a natural fit. And I, and I, I did lead a recapitalization of a rapidly growing platform in the Northeast in January, 2020. So that was wonderful timing, right before covid. That's

Pete Moore (04:44):

When it closed the original.

Eric Epstein (04:45):

Yeah, we, we closed that January, 2020 and, you know, there were, there was a number of H V L P deals that were done right prior, right prior to covid. And so, you know, a lot of our initial excitement and enthusiasm quickly waned, you know, 60 days later Sure. 60 days later. And I have some other colleagues within private equity who also closed deals within a short period of time of the onset of covid. And we traded a lot of war stories you know, throughout the initial term of covid. And thankfully, you know, most of us, particularly within H B L P, have bounced back quite nicely. But, but obviously that's only one area within, within Halo. I mean, I love enthusiasts, consumer brands and other just, you know, rapidly, you know, rapidly growing brands that have, you know, a real franchise around them. And so mm-hmm. <Affirmative>, what, what does that mean? That means it's something that isn't just a fad. It's something that has a nice growth curve and, you know, adoption curve to it, and something that has good gross margins and becomes scalable over time. And something that is more than a product, you know, hopefully a, a product line where you know, you have a real opportunity to build, build, you know, build a real business.

Pete Moore (05:58):

Yeah. So, you know, as you take a look at what happened in the Planet Network where entrepreneurs bought up area developers, once they bought that development territory, they started to borrow money, personal guarantee it, open up 10 or 15 leases personal guarantee it, and then private equity says, Hey, that these unit economics look pretty interesting and you got a, a territory that you own exclusively as planet, you know, was kind of the first to say like, Hey, it's kind of like a cash register and it's not that hard to run because I'm not running any group X I'm not running any personal training, I'm not running any daycare, I'm not running any pro shop. You know, when private equity looks at that and says, Hey, look, I want to go and partner with one of these a CEO, you know, from your standpoint as being an independent sponsor, you know, you've got some, you know, pros of like, Hey, partner with me because look, I'm gonna be along on the ride here with you.

(06:50):

I'm gonna help you manage this business. I'm gonna help you interface with a private equity. Or my investors talk about the difference between like a private equity firm doing an area developer deal and like Planet or Crunch. And you as an independent sponsor cutting a deal and then going out and getting the capital. But you staying on with the deal is almost like obviously a board member, obviously like an intermediary to an extent. Yeah. And also like a buffer and a benefit to the management team where it's like, Hey man, you don't have to do a private equity deal. It's like you and the private equity firm, I'm actually here as like a conduit and a bridge that's gonna help raise the probability that we're gonna get through whatever we need to get through together. Yeah. How do you think about that? Or, or,

Eric Epstein (07:31):

Yeah, here's, here's how I would answer. I actually operate a little differently than most independent sponsors. What I don't do is I don't court a founder or a management team and try to lock up a deal and then go dial for dollars, what I actually do.

Pete Moore (07:45):

No, I wasn't implying that. No,

Eric Epstein (07:47):

No. But that's what most in, but

Pete Moore (07:48):

That's a point, that's

Eric Epstein (07:48):

What ahead most independent sponsors have. I actually operate a little differently, which is I go, look, you know, all of these, all of the processes I'm involved actually are not processes the processes, it's a courtship process because the vast majority of transactions in which I pursue are, you know, they're all relationship based or cold calls or cold emails where relationships were established over, you know, years, months, if not years. Right? And so what I do is say, Hey, look, I'm interested in helping you recapitalize your business or acquiring your business, and you know, what are your goals? And by understanding your goals, I can help, I can help bring alternatives to the table. And what I'll do is I say, look, again, rather than locking you up into a deal and then dialing for dollars and trying to get that deal financed, yeah. What I do is I bring various alternatives so that the founder or management team or owner can make a decision as to, Hey, this is, that's interesting. This is what's most ideal and best for me. And then say, okay, I can, this is, I can get that. What I'll do is I test the market on a very curated basis. And so I, so I bring back what the market has to, so

Pete Moore (08:53):

Kinda like a hybrid between like, I'm your advisor and your banker, and I'm also like your independent sponsor option,

Eric Epstein (09:00):

Right? So

Pete Moore (09:00):

I think with a private equity fund to say like, lemme show you like the buffet, right? And I'm, I'm not fronting that my buffet is gonna be the winner. I'm like giving you what the market says. What

Eric Epstein (09:09):

I try to do is say, look, here's, like, as an example, here's maybe a majority option. Yeah. And here's a minority recapitalization option. And I will sh I, I'll sh I'll speak to the right number of parties, and I might be three or five parties under either option so that we can present options and people to say, look, I like this, or, I like that. And then, and then I will work with these various groups to present, you know, alternatives to, again, a founder or management team so that they can pick what's best for them. And it, but unlike a banker, I stay involved. So I, I co-invest in the deal. I sit on the board, like on the Crunch Fitness franchise that I'm involved in now. You know, I'm on the board. I act very much as kind of a coach, mentor you know, to our, to our co I act as our cfo. I deal with all our capital markets, and I'm, you know, the interface directly with our, you know, family offices and institutional capital partner that, that is involved in our platform.

Pete Moore (10:04):

Gotcha. So, you know, as you take a look at going into Crunch, let's talk, talk industry wise, you got in into January, 2020, not great timing. However, you know, you did have a, a partner in, in Seacoast, and I'm sure they have the, the word flexible on their website. A lot of guys weren't flexible during covid and, you know, when they stopped getting paid. So how did you, how do you think about, you know, picking your partner with people that have done multi-unit in the past, people that you have relationships with, what, what's your criteria to say to that entrepreneur, Hey, here's all your options. If you do a deal with me, I'm gonna do a deal with a group that is like-minded, or it's not just

Eric Epstein (10:43):

Yeah. Well, that's, that's a good que question. And one of the things, you know, that, that I share with people is, look, as I present alternatives, you know, economics a part of it, but there also has to be a good cultural, cultural fit. Because most of the transactions I focus on are more, they're, they're, they're gonna be more of a partnership rather than an entire sale or bio of a company. And so I said, look, you're not just selling your company for the highest price and moving on, you're entering a partnership. And so, you know, understanding the terms of that, not just economically and structurally, but just kind of culturally is, is a big deal. And so, fortunately as you know, there's no shortage of investors who are interested in getting into this space. And so, you know, we have, you know, we collectively have relationships with many, many, but we know our, there's a short list of folks in which we think will be the right fit for any particular situation.

Pete Moore (11:31):

And, and that they've also looked at other deals. And you don't have to get up to speed with that on the entire

Eric Epstein (11:35):

Industry. People that know the sector you know, people that have the, have the experience in sector and also people that have had challenges in this sector because, you know, as you know, everyone's a great partner when things are going well, but, you know, you really find out how good your partners are when things, when you're, when you're challenged. And so, you know, we were just talking a second ago, you, you brought up the fact that Seacoast Capital is the institute, my institutional capital partner on our Crunch Fitness franchisee. Seacoast is an unbelievable partner. I mean, they, you know, they basically financed the minority recapitalization of 21, you know, crunch locations in January, 2020, and everything was going, you know, fantastic for 45 or 60 days until the world shut down. It's

Pete Moore (12:16):

Like short, shortest private equity honeymoon <laugh>.

Eric Epstein (12:18):

Yeah. Well, there, I had, there's a couple examples of, look, the, the, the Prospect Hill Crunch platform. I think those guys closed you know, later in January, beginning of February. So they, they actually <laugh>, they actually flew even closer to the sun, the Covid Sun. But you know, to your point, the, like, Seacoast, they, they funded half their investment in closing and half their investment really subsequent to closing. And they, they adhered to the terms of the original deal. I mean, talk about amazing partners. I mean yeah. You know, just patient flexible backing you in tough times. I mean, those types of partnerships, that's not what you find across the board as you know. Yeah. And so, you know, people like that obviously have the long, the long view relationships are important, integrity's important and just maintaining their word. And so they've been an unbelievable partner. And obviously someone I would grab would, would partner with rapidly, eagerly again. Yeah.

Pete Moore (13:12):

One, one of the things that I've seen over the years that has gone wrong with private equity funds doing deals with management teams or, or an owner and the, and the private equity fund ends up buying majority control or like 49% control, whatever it is, the, the, the CEO of the company thinks that they rented capital and the private equity fund thinks that this guy or this woman's under an employment agreement. Yeah. And I feel like if you don't understand what the relationship is the day after closing, you're probably gonna at some point butt heads of like, Hey, am I running money for you or are you working for me? Cuz I'm running the money. So how do you, how have you kind of like laid out and establish like, Hey, this is how shit's gonna go.

Eric Epstein (13:58):

It's a great question. I mean, look, it's all about managing expectations. It also picking, picking good partner. But I mean, I, there's, I can think of very, a lot of very successful private equity transactions, either majority or minority deals where the partnerships have been, have worked out unbelievable in good times and bad. Yeah. And then, but I also, you know, I'm very familiar with situations where actually, as you alluded to just the, you know, the perspective of the, the private equity now owner and the manager, the, you know, entrepreneur or CEO who now feels like more of an employee than that entrepreneur or majority owner in the past. Those you know, there's, there's a conflict over time. And you know, you know, things, I think of an example of a, I have a very good friend of mine who sold a business in the, in the healthcare space who you know, very successful exit sold 60 or 70% of the company to a very well-known private equity fund. And within 12 months of closing a deal, they're butting heads and, you know, the CEO stepped down and he still owns a ton of equity, you know, stay on the board. But you know, the, the relationship dissolved really quickly. Yeah.

Pete Moore (15:09):

I feel like, I feel like ownership disputes tank companies more than like management like strategy dispute. I feel like once there's like a, like a toxicity at the, at the board level, it kind of somehow like drips down like a flood. Like a flood.

Eric Epstein (15:27):

Well, yeah. I don't know if I could compare the two, but I, you know, there's plenty of examples of look, if you have a, if you don't have a healthy collaborative, cooperative environment at the board level, it's gonna cause problems. We actually have a very interesting board dynamic at our, at our crunch platform. We have a, a really d a disparate minority shareholder base, meaning we have two large family offices and one institutional capital partner, plus a CEO who, who exchanged, you know, he sold his company into our platform. And so in exchange for a bunch of equity, so we actually have four very large yet minority equity holders, and somehow our board in corporate governance works mm-hmm. <Affirmative>. But I'd say that that's, that dynamic is unusual. But it is, it is collaborative and it, it works. But, but obviously, you know, those relationships, if they, if they dissolve it that toxicity can, can filter down real quick.

Pete Moore (16:28):

Yeah. Let me ask you two more questions. And obviously you, you and I can riff for hours here. But I really want people to understand and get, get a couple of takeaways from private equity, the benefits of doing it, the, the, the professionalism you get. The one thing I want to ask you about is, you know, there's a lot of franchisors out there that, you know, want to become the next massage envy and want to become the next Orange theory. You know, you could say F 45, like, oh, like they were gangbusters. If you saw that public company stock, you'd be like, oh, I'd love to be a franchisee of F 45 until you actually did the work. Right. And realize that you don't want to become one, right. Cause the unit economics don't work. So, you know, over the years of doing this, how much do you trust your gut or like interview like, or read through like, hey, who's the franchisor, who's like my ultimate parent company partner?

(17:15):

Cuz you've got a really interesting, you know, almost like a, a rectangular relationship between like landlords, franchisor, franchisee and equity group, and probably a debt group in the middle. It's almost like an oc, you know, a hexagon or something about all these relationships. So how do you think about diligence in a franchisor as a, as a sponsor, as a private equity firm, as a manager and be like, Hey, I don't know if I trust these guys like Planet Fitness back in the day, you go up there, they had like a beer keg and they had like, you know, calendars. You'd be like, dude, I don't know, man, this is a little bit crazy for me.

Eric Epstein (17:48):

Look, I think look, you ask a good question, particularly now where the franchise model is so popular, right? Yeah. And so it's, it's, it's expanded so greatly within health and wellness, you know, on the, on the success of everything from planets to, to exponential. Look, the, the diligence on the franchisor is that that's, that is an important part of diligence. I mean, look, as a franchisee, you have, you have a playbook, you have your territory and you have, you know, you have to really, you better like that playbook and you better like the, the folks that drafted that playbook and you better, you better, you know, those unit economics better work and that playbook has to work. And so if you're not comfortable with, you know, kind of the genesis of that, then you have an issue. Now, fortunately I actually met Mark Soff and Jim Rowley many, many years ago and had a great deal of respect for what they've done in this industry Yeah. And how the industry is involved over time. And so I felt like I had a leg up because of a preexisting relationship where I was comfortable with them as, as individuals and could, you know, and they also were very, would give the time upfront to answer questions for myself and our capital partners so that everyone was comfortable with That's great. What our strategy was and where, what our goals were within our market.

Pete Moore (19:01):

Yeah. And then, you know, as you think about, you know, exits and you think about, you know, the time horizon, north Castle just did a deal where they basically wanted to hold on to their portfolio company and then had a continuation fund. There's several of those types of deals where there's a Planet Fitness, big Planet fitness franchise area developer that private equity firm doesn't wanna let go cause it's great business. Right? So how do you think about maybe like in this new private equity environment and maybe more traditional business norms with higher interest rates, maybe less economic growth maybe like a 10 year hold isn't like a crazy idea if you got a really good business instead of going and selling this one and going, trying to find another one.

Eric Epstein (19:45):

Yeah. Well, I, I fully agree with that. I mean, I think, you know, one of the, one of the deficiencies in the private equity model is that pressure to, you know, sometimes monetize prematurely because of just the fund raising cycle. So I actually agree, when you have a good business and you continue your growth trajectory, or maybe you're just operating in harvest mode, if you have a good business with good unit economics you know, unless you're forced to deploy that capital elsewhere, I'm, I, I am a big fan of that long-term hold. Yeah. And so for something like this, in, in my situation, as I mentioned earlier, we have this disparate minority shareholder base where I have different shareholders who very likely have different goals and timelines, right. Which we will respect. And so my, honestly, one of the jobs I, I do is as you know, kinda like acting CFO and dealing with all our capital markets and in, in presenting various options over time to, to our partners is, look, the CEO and I, we love doing this.

(20:41):

And we we're very much, you know, right now we're 34 locations. You know, my gut tells me, you know, we're gonna open up eight locations this year. We have some m and a in our pipeline. So, you know, we should be, I'm hoping we're at 50 locations within the next 18 months or so. We got a lot of fire in the tank. Yeah. But some of our investors may have different goals and timelines. So my only goal is to make sure that we always have one, a capital structure to support our growth plan. And two, also have the, you know, have the capital structure in place to provide our shareholders options over time in the event if and when they wanna exit over time. And the CEO and I, we say it to ourselves all we tell our each other all the time, Hey, so long as this is fun, we'll keep doing this. Yeah.

Pete Moore (21:23):

So, no, it's great. That's great. Well, let's make this part one of our of our multiunit series of let's Do It podcast. So we bought, banked our first 20. Good to see you again in person. Hopefully we'll work out some deals together. Let's do it. And welcome to the Halos Sector in a big way, and if you've got questions about how independent sponsors works, private equity, and you want a second opinion, I'm gonna, I'm gonna sit you up with Eric, so please do. Good stuff, man. Good to see you. Thanks

Eric Epstein (21:51):

Pete.