Bus Manufacturer Sale Arrives Right on Time

KPS Special Situations is flying high after successful turnaround of New Flyer

BY ART JANIK | Just as the wheels on the bus go round and round, so does the heavy-duty bus manufacturing industry.

Transportation equipment manufacturing may not be the most exciting ride for private equity, but the stability of the sector's replacement cycle for heavy-duty buses, as well as a slow, but steady growth in bus ridership in North America, means a consistent market that depends on companies who specialize in vehicle replacements and upgrades. Municipalities also receive most of their funding for buses from the federal government, and since buses have a maximum 12-year, or 500,000-mile, lifespan, bus manufacturers are guaranteed continuous orders.

Last month, New York-based distressed investment specialist KPS Special Situations Fund capitalized on its recent investment in the bus manufacturing sector when the firm sold its controlling stake in Winnipeg, Canada-based bus manufacturer New Flyer Industries to New York-based Harvest Partners and New York-based Lightyear Capital. Although the exact figures in the deal were not released, press reports speculated the transaction to be worth more than $300 million. Harvest Partners led the investment, which is slated to close in the first quarter of 2004, with Lightyear acquiring a minority stake.

New Flyer is the largest independent manufacturer of transit buses in North America, with annual sales of more than $470 million. In addition to its Winnipeg headquarters, the company has two additional production facilities in St. Cloud and Crookston, Minn. New Flyer produces the low-floor and articulated city buses operated by public transit authorities in many major metropolitan areas in the U.S. and Canada, including New York, Los Angeles, Vancouver, Atlanta and Seattle. The company's business model involves outsourcing vehicle parts and keeping the production facilities' focus to bus design and assembly.

New Flyer was founded in 1930 as Western Auto and truck Body Works Limited and produced truck and bus bodies. Following a series of transition, in 1971 the company name was changed to Flyer Industries Limited, which developed and sold large heavy-duty transit bus models. In 1986, the company was acquired by Den Oudsten, B.V., Holland's largest bus manufacturer and became New Flyer Industries.

New Flyer today designs and sells a line of urban transit diesel buses in 35', 40' and 60' lengths. The company developed and introduced to North America the "low floor" bus, now an industry standard. The company is currently developing buses with new engines that run on compressed natural gas and liquid natural gas, which do not produce the noxious exhaust of diesel. New Flyer is also working on diesel electric hybrid technology.

KPS, whose private equity funds focus on companies in the manufacturing sector that have a strong franchise and a solid product line, but are facing some form of operational or financial problem, originally bought New Flyer back in March 2002 for C$44 million (approximately $27.5 million at the time), partnering with founder Jan den Oudsten, and brought in new management, including chief executive officer John Marinucci. KPS also worked with the province of Manitoba to keep the company's head office and half of the company's employees in Winnipeg in exchange for a $C20 million government loan. The firm's investment was the catalyst for a financial and operating restructuring that also involved the support of the company's banks, the Communications Worker of America, the Canadian Autoworkers Union and the company's key suppliers.

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"New Flyer had reached a point of crisis, and so we stepped in," says KPS managing principal David Shapiro. "Our firm's mandate is to shepherd those types of companies to a point of stability where subsequent investors can take over and grow the company from a stable base, grow it into the type of company it was meant to be."

Shapiro says his firm learned about New Flyer's situation after KPS was approached by Deloitte and Touche, whom New Flyer had hired to represent the company in its search for outside equity funding. Prior to its sale, the company had gone through a series of plant expansions that landed the company in an operational and capital crisis. In March 1996, New Flyer

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Financial Sponsor Backed Exits and Offerings

December 2003

This chart displays the number and value of global financial sponsor backed exits and securities offerings during December 2003, according to Capital IQ. The data is divided by sector and includes both buyout and venture capital firms. This data is intended to help market participants follow exit and refinancing activity sponsored by private equity firms. Values are in $mil. Learn more about Capital IQ at www.capitaliq.com

December 2003

	No. of Deals	Value of Deals
Energy	n/a	n/a
Materials	5	$3,113.71
Industrials	22	$1,412.93
Consumer Discretionary	11	$1,116.28
Consumer Staples	4	$1.39
Healthcare	6	$206.43
Financials	4	$165.75
Information Technology	9	$681.07
Telecom Services	n/a	n/a
Utilities	n/a	n/a
TOTAL	61	$6,697.56

Year to Date 2003

	No. of Deals	Value of Deals
Energy	25	$1,926.12
Materials	69	$11,483.64
Industrials	266	$34,577.79
Consumer Discretionary	159	$16,469.12
Consumer Staples	27	$2,274.11
Healthcare	69	$3,346.82
Financials	42	$3,389.85
Information Technology	117	$7,558.83
Telecom Services	2	$370.08
Utilities	1	$0.00
TOTAL	777	$81,396.36

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relocated to an assembly facility in Crookston, Minnesota. In 1998, the company's continued growth required the construction of a third assembly plant in St. Cloud, Minnesota.

Shapiro says the company grew too quickly and borrowed too much without the operational expertise to handle all the sudden changes. Although demand for New Flyer's products and services was high and the company needed to increase capacity, it had trouble bringing the plants online and integrating them with the existing business.

"Performance suffered, and as a result the company had to borrow even more money," Shapiro says. "The working capital situation got out of control, and New Flyer lost the confidence of its lenders. It lost access to bonds, which is required when bidding on municipal contracts. We came in to see what we could do on the operating side to reduce the bottlenecks and problems."

Shapiro says KPS proceeded to unblock capital issues, renegotiate credit agreements with the banks and labor contracts with current employees and infuse fresh capital from both the firm and the provincial government. KPS also brought in new management, including the firm's own CEO, head of operations, and engineering team that managed to turn the company around in less than two years and was a big reason for the Harvest and Lightyear investment.

"The management team at New Flyer, led by Jon Marinucci, was a good, solid team, good folks at all levels," says Harvest senior managing director Ira Kleinman. "As is usual with our deals in private equity, we always look for quality and depth of leadership."

In addition to good management and the bus industry's cyclical replacement schedule, Kleinman says New Flyer's backlog-based model gives a better cash-flow perspective than most other traditional businesses. Product orders are set a year in advance, allowing a better vision of what sales figures will look like twelve moths down the line.

Shapiro says the deal was an example of "consensual restructuring" - working together with all the parties involved and not forcing any drastic changes. He says he was especially impressed with the company's founder, an exceptional bus designer who truly cared about the future of New Flyer's success.

"That's bringing all the parties together and trying to work with people - not forcing anything down people's throats," Shapiro added.