

Buyouts

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Thayer Capital's Saga Deal Tells A Compelling Story For Software

By Christa Fanelli

If firms and companies were people and life was a movie, the story of **Thayer Capital Partners**, **Saga Software** and **Software AG** would be an award-winning, well, saga . . .

Once upon a time, Germany's Software AG, wrought with internal problems, reluctantly gave up Saga Software when it could no longer sustain the two companies as one. Thayer Capital, a private equity firm from a land far, far away (Washington, D.C.), came in and picked up the fragile remains of Saga. Saga and Thayer dedicated themselves to making the company strong again, and the effort succeeded beyond all expectations.

Then, the market changed. Saga once again faced tough times, only to find that Software AG had turned itself around and wanted Saga back. With a tear in its eye (well, really a nice return on its books), Thayer bid Saga farewell, and Saga Software and Software AG were reunited.

While the story reads like a stan-

dard hello-goodbye-hello tale, Saga's journey is far more interesting when you take a look at the characters and observe in greater detail just how the plot unfolded.

Software AG, a large German mainframe software company started in 1969, was a giant in the business in the 1980s, even overshadowing **Microsoft** at one time. Its databases supported such businesses as the **MCI** friends and family program and **Morgan Stanley's** trading operations. But about six years ago, things began to go awry. The company's chief executive officer and founder began to move Software AG into rather obscure areas of technology, and the company began to lose money. By 1996, the company had approximately \$100 million in bank debt and the board decided to replace the original CEO. **Erwin König**, the new CEO, joined Software AG only to find that the bank lines were due in five months and the company was in desperate need of capital.

On the other side of the Atlantic at Saga Software, then a subsidiary of Software AG, CEO **Daniel Gillis** and CFO **Harry McCreery** were gearing up for a possible management buyout of their company, which had once before been independent. "The U.S. management team were close observers of everything that was happening in Germany," says **Rick Rickertsen**, the chief operating officer at Thayer Capital. "They saw what was happening in Germany, and they thought they may have an opportunity to buy the business from the Germans to get [Software AG] some capital to pay off their bank lines and also to get control of their destiny in the U.S."

In an effort to find someone to back the MBO, Gillis contacted **Phillip Norton**, the CEO of **ePlus Inc.**, a Thayer Capital portfolio company for which Rickertsen is a board member. Norton arranged a meeting between Gillis and Rickertsen, and the buyout was underway.

"We were off to the races at that point," recalls Rickertsen. "Dan really thought he had a great shot at buying this business, and I agreed. I had known Software AG going back to 1983 when I had worked in Morgan Stanley's high technology group and knew it was a good business. And I really liked the management team and thought this would be an exciting opportunity for us to back these guys."

Thayer Capital had been targeting the technology services and software sector in Northern Virginia at the time, and Saga Software, based in Reston, Va., fit the mold.

Indeed, it was a race against time for the three players in the deal. Software AG's bank lines were due on April 1, 1997, and the deal only got started in January 1997, which gave Thayer only 70 to 80 days to close it.

Under terms of the agreement, Thayer agreed to buy Saga Software — then known as **Software AG Americas** — from the German company for \$85 million, which was 8.5 times trailing pre-tax profit at the time and approximately five times the projected 1997 pre-tax profit based on management's projections.

But just when everything seemed to be moving along smoothly, the deal came to an abrupt halt. "Two weeks before we were supposed to close, our senior lender walked away from the deal, which gave everybody a heart attack," says Rickertsen.

Apparently, the unnamed lender's credit committee was weary of investing in software companies. "We said to them, 'Gosh, it was a software company a month-and-a-half ago when we started working on this

project. It would have been nice if you had told us that your credit committee didn't like software deals,'" Rickertsen says.

Luckily, McCreery, Saga's CFO, was able to save the day. He managed to secure financing from **Sanwa Bank**, which he had worked with before. And despite the last-minute obstacles, the deal closed on April 1, 1997, just as planned.

Thayer Equity Investors III LP contributed \$30 million to the deal giving, Thayer 75% of the company. Sanwa Bank provided a \$55 million senior revolving facility. The Saga management team took approximately 16%, and Software AG retained approximately 10% of the company and a board seat.

The Comeback

Once free of its ailing parent company, Saga Software was quick to recover, and the new owners had big plans for the company. "The large-scale database systems are pretty low growth," says Rickertsen. "So we wanted to do some acquisitions and get into a higher-growth area and leverage this great customer base. The company has an absolute blue-chip list of customers."

Keeping its promise, the company's first add-on came just six months after the buyout. Saga Software in September 1997 purchased its Canadian distributor, **R.D. Nickel & Co.**, for \$12 million.

In fact, the company had been progressing so rapidly that it was already ahead of its projections. "The management team was doing a fantastic job improving profitability — a tremendous job," says Rickertsen.

"During that first year, instead of doing \$16 million pre-tax profit [as they had projected], they did \$22 million of pre-tax profit."

Looking Ahead

At the time Thayer purchased the company, the firm tossed around exit strategies — namely, an initial public offering or a sale to a strategic buyer. In 1997, the public market was strong, and three or four investment banks had responded well to the idea of an IPO for Saga, so Thayer began to take that possibility seriously.

On Sept. 26, 1997, Saga Software filed for an IPO led by **Robertson, Stephens & Co.** Then on Nov. 18, Gillis, Rickertsen and the Saga gang stood in front of the **New York Stock Exchange** and banged the gavel as the company went public, offering 7.7 million shares for \$10 per share. Just eight months earlier, Thayer's investment had been at \$1.47 per share.

With the IPO, Thayer reduced its stake in the company to 65%, taking out \$30 million — the equivalent of its initial equity stake in the company. On its first public day, Saga Software's stock opened at \$11 and closed at \$10.50. Four months later, it was back for a secondary offering at \$24.25 per share.

Moving forward with its plans for acquisitions and higher-growth products, Thayer Capital in late 1998 purchased **Blue Lobster**, an enterprise integration software company, for approximately \$12 million. Enterprise integration software is "middleware" that links mainframe systems with the Internet and client servers. The Saga owners thought

this was a good match for the company and soon introduced **Sagavista**, an enterprise integration product line.

Saga Software continued to improve its business and 1999 turned record profits for the company due mainly to the jolt in IT purchases related to Y2K preparation. Its pre-tax profits reached \$45 million, more than twice what it was in 1997, and revenue grew to approximately \$250 million from \$170 million at Thayer's time of purchase.

Then 2000 came along and, like all technology companies, Saga found

ment team, which was uncommon in Germany at the time. "He really did an unbelievable job with the German company," says Rickertsen. "He took it public. He raised a ton of money and he took his business — which was almost broke when he sold us the American company — and made it extremely profitable by cutting costs."

Throughout its involvement with Thayer Capital, Software AG always held on to the idea of buying Saga back at some time. "We had exclusive rights to the U.S. and Japanese software markets for all Software AG

much impossible for a board to turn down that type of deal," says Rickertsen. "So we accepted the deal."

With **Update Capital**, a niche investment bank in the software sector, advising Saga Software, the company was sold back to its parent company on Feb. 1, 2001, and its name was changed back to Software AG.

Unlike the complaints often heard by private equity firms dealing with foreign companies, Rickertsen says the whole process was very smooth. "[The Germans] are reasonable people, [and] they were motivated to get a deal done," he says. "While they were minority shareholders, they were quite constructive. When it came time for them to buy the company it was a challenging negotiation, for sure, and they took advantage of a very tough technology market in the U.S. On their part, it was a smart buy."

It was not too shabby of a deal for Thayer Capital either. The firm had a gain of \$250 million on its \$30 million investment, recovering \$280 million over the lifetime of the deal. The internal rate of return on the deal, including the IPO and final sale of the company, is a whopping 459%.

The success of the deal is not lost on Thayer Capital. Rickertsen says he does not have a single regret with this transaction. "It was a really great transaction, and it was great to see this management team do so well," he says. "They're a really high quality team, and it's just one of those rare circumstances where most everything breaks your way in a deal and everybody wins."

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that the days of rocketing stock prices could not last forever. The company missed its earnings estimate for the first and second quarters, and the stock dropped to \$5.50 per share before the first half of the year ended.

Happily Ever After

Meanwhile, back in Germany, Software AG CEO König watched the success of the Saga IPO and decided to follow its lead. In 1999, Software AG went public on the Frankfurt Stock Exchange and turned itself around. Additionally the German company arranged for an equity interest for the manage-

products and [König] always wanted to get back into those markets," Rickertsen says.

With its new-found financial health, coinciding with a sudden downturn in the American stock markets — particularly for technology companies — that day was drawing nearer. When Saga's stock, which had at one point reached \$32 per share, dropped to about \$10, Software AG offered to buy the company back for \$15 to \$16 per share. Then Saga's stock price dropped again to \$5.50, and König offered Thayer \$11.50 per share in cash. "That was over 100% premium from where the stock was, so it's pretty



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