

Reprinted from THE WALL STREET JOURNAL.

WEDNESDAY, AUGUST 25, 2004

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Texas Start-Up Blue Sage Capital Survives Drought

BY BOB SECHLER

DOW JONES NEWSWIRES

AUSTIN, Texas -- A drought-resistant wildflower -- blue sage -- seemed an apt metaphor to Peter Huff and two partners in November 2002 when they first began raising money for an inaugural private-equity fund. It took time, but their optimism proved well founded.

Blue Sage Capital announced this summer that it closed a \$170 million fund to buy out or provide growth capital to established small and midsize regional companies, although Mr. Huff said the bulk of the fund raising was completed by the end of 2003.

Billing itself as a regional, small- to middle-market fund, Blue Sage aims to invest \$5 million to \$10 million in profitable companies throughout Texas and contiguous states over the next four years.

Mr. Huff said the \$170 million came in \$70 million higher than his newly minted firm initially targeted.

"It was a very negative, pessimistic fund-raising environment" when Blue Sage first began looking for money, Mr. Huff said. "But we actually saw that as a positive, because there was less competition."

He and his partners, Jim McBride and Bo Baskin, had other aces in the hole, as well. For one, all are well connected and highly regarded in the central Texas investment community, and that helped to win some big-name investors.

Mr. Huff is a former partner at Austin Ventures, the largest venture-capital firm based in Texas. Mr. McBride formerly managed LBJ Holding Co. -- the private-investment arm of the family of President Lyndon Johnson -- while Mr. Baskin was chief executive of Baskin Family Camps Inc., which operates Texas and Colorado summer camps and corporate conference centers.

Blue Sage's initial investors included LBJ Holding, which kicked in \$20 million to \$25 million, although Blue Sage declined to disclose the precise amount.

The firm also raised money from institutional players, including Bank One Corp., which since has merged with J.P. Morgan Chase & Co., as well as Wells Fargo & Co. and Washington Mutual Inc. In addition, the federal government's Small Business Administration invested in the fund, as did state economic-development entities in New Mexico and Oklahoma.

"We're generalists by design, so we're not specifically seeking out any particular industry," Mr. Huff said. While he expects Blue Sage's portfolio to be "eclectic," he cited one industry -- technology -- in which the firm is unlikely to invest heavily, saying valuations in the sector still appear too high.

Meanwhile, observers of the Southwest's private-equity market say they aren't surprised by Blue Sage's fund-raising prowess despite the slow economy, citing the solid backgrounds of the firm's partners.

But some expect Blue Sage to encounter significant competition for good deals, because the market for established companies has become increasingly crowded in the years since the dot-com bust.

"The whole [investing] world has gone from extreme risk-taking to the opposite end of the spectrum, where even early stage [venture capital] firms are moving into the buyout arena," said Bruce Ezell, a managing director at Austin VC firm Techxas Ventures.

Eugene Lowenthal, a partner in the Austin office of investment bank Growth Capital Partners, based in Houston, concurred, saying the investment market for small and midsize private companies "is probably a little bit overcrowded in Texas."

Blue Sage's first investment, announced in late June, is typical both of the type of deals the new firm considers its specialty and of how it expects to find them. Blue Sage bought a 55% stake in 30-year-old Environmental Design Inc. for an undisclosed amount after one of Mr. Baskin's friends told him that founder and President Tom Cox was planning to seek liquidity.

Environmental Design, based in Tomball, Texas, outside Houston, is a leading tree-transplantation company, providing large trees for new land developments, such as golf courses and resorts.

"This business has been very profitable for a long time," Mr. Cox said. "It really has the wind at its back" because of the environmental movement and a recognition of the value mature trees add to real estate.

Mr. Cox said he liked Blue Sage because it didn't take a short-term view of its investment in his company and because the deal allowed him to remain heavily involved.

Blue Sage plans to hold its investments an average of four to seven years, Mr. Huff said, with a merger or acquisition the most likely exit strategy.