Interview: Adam Coffey
CEO of CoolSys
Author of The Private Equity Playbook
Interview on 08/11/2020, at 11:30 a.m.

Mike Nappa
Today is August 11th, 2020. We are here with Adam Coffey, CEO of CoolSys and author of the book, *The Private Equity Playbook*. I am so glad that you're able to take time. Adam. I read your book here a little bit earlier this summer and I'm like, this is a guy that I need to feature. This is a guy that I want to talk to our readers. So I appreciate you taking time.

Adam Coffey
I appreciate your interest.

MN
The way this will go is, I have a short set of interview questions that I'm just going to let you ramble on about, and then when we get to the end of this—now, are we a hard stop at noon?

AC
I can run over a little bit if you can, since I'm reason we're late.

MN
I promise not to take more than 30 minutes total. At the end of this, about the last five minutes, we're going to do what I call The Dirty Dozen. I'm going to ask you some questions and you just say the first thing that pops in your head. We're going to go through 12 of them in in 5 minutes.

AC
OK.

MN
So we gotta start this interview with Virgin Galactic SpaceShipTwo, right? You gotta tell me that story. Come on.

AC
You know what? Life is a set of experiences and throughout my life I've been fortunate to do many things. I'm a veteran, served in the US Army. I've been a CEO, a bestselling author. I'm a pilot aircraft owner, and I thought boy for an ex-military guy who's a pilot what would be funner than being in your mid 50s and going into space. So as soon as Virgin Galactic decided to take deposits, I thought, "This is one life experience I need to add to my list."

MN
That's awesome. When do they expect to go?

AC
I have no idea. I was joking that Tesla announced the Cybertruck was taking deposits, as is Virgin Galactic, and so I have a deposit on a Tesla Cybertruck and I have a deposit to go to space with Virgin Galactic. So the real million-dollar question is, which comes first? My ride in space? Or my Tesla Cybertruck? I'm going to probably bet on the Cybertruck, which I'll drive then across the desert to get to New Mexico to the launch point. But I did see Virgin Galactic just did a public offering and raised almost half a billion dollars to help fund that dream of getting me into space.

MN
That's awesome. Alright, our readers are people like you executives and mid-market companies. Thinking about the Private Equity Playbook, which was very helpful to me, by the way. I found it very interesting. In thinking about the Private Equity Playbook. What would you like those executives at mid-market companies to know about you and about this book?

AC
Well, so I've spent the last 20 years working in private equity, building companies for private equity. I’ve built three different national service companies, and I'll have to admit that back when I started on my journey 20 years ago, I had no idea what private equity was. Even to this day most people in the Fortune 500 world, or most small businesspeople have some kind of a connotation about private equity, but it's not necessarily the accurate one, or the correct one.

I think usually when you hear about private equity in the news, people tend to be negative. “Some rich guy made a ton of money on the backs of destroying a bunch of companies!” and that's just not what private equity is all about at all, from my perspective. I built three large companies, employed thousands of people, and they're growing. All three of them grew at very fast paces. So from my perspective, with private equity now almost 5 trillion dollars in assets under management, continues to grow since the publishing of my book, and with more than 5500 private equity firms now on the planet, literally half of all merger and acquisition activity on the planet involves private equity on one side or the other.

So with the explosive, explosive growth of private equity, I wanted to write a book to serve as kind of a basic introduction of very broad scope. It covers many facets of private equity, what private equity is, and what it's about. And then more importantly, from a business owner or an executive perspective, how should you think about private equity if you've built a company and your contemplating monetizing that asset? How do you make sure you’re partnering with a good private equity firm? And if you're a Fortune 500 guy and recruiters keep calling you to come run a private-equity-backed company, what does that mean? How does it work? How should you think about it? What questions should you ask?

So I just decided that there was this big vacuum and at the time when I started writing the book. If you did a search on Amazon for private equity—there's 1.8 million books on Amazon at any given time—and there were literally only a handful of books about private equity at the time. I thought boy, this book is long overdue. I can take 20 years' worth of life lessons, mistakes, and learnings, and pass that on in something that you could read in about 3 1/2 hours. There was a very specific reason I picked that time frame. I wanted you to be able to jump on an airplane in New York and have a drink, eat a bad meal, and then settle back in and be able to finish this book before you landed in Los Angeles or vice versa. So it was it was very wide in breadth, not very deep, because every time you go deep in any subject you wind up in a rabbit hole that could be its own book. So I wanted to keep it high level but wanted to give a broad understanding to people who were business owners and Fortune 500 executives, and people who were hearing about private equity and interested in or being approached by private equity. I wanted them to have a very good understanding of what it was that was going on in that world.

MN
Well, I think you accomplished what you intended. Book was good, easy to understand and follow even in some complicated subjects. One of the things that you highlight in the book, I think you said it a few times was, "why sell your company once when you can sell it 3 times?" Can you tell us a little bit about that philosophy?

AC
A lot of times business owners, or founders, build companies and then they think of monetizing the asset as a one-time transaction. So I built this company. Maybe it's got $10 million in EBITDA, maybe it's got $70-80 million in revenue. Or maybe it's much smaller—pick a size doesn't matter. But people think, "I built this thing. It's time to cash out my chips." And they just totally think about it from the perspective of who's the highest bidder? Who gets me the biggest payday? And off I ride into the sunset.

I've earned a living, created generational wealth by understanding how private equity works. And again, if you understand how private equity works, you know that any enterprise backed by private equity is going to be sold every three to five years. So as that company continues to grow, you can get multiple paydays. So what I started thinking of it was in terms of taking [only] *some* chips off the table when you sell your business. Maybe you're approaching that age. You're in your 50s now and you're starting to get nervous about the future. So you can partner with a sophisticated private equity group, sell the business, but maintain ownership in the company by doing a rollover investment.

Let's say—using some example numbers that are real examples of a company that I bought three years ago as an add-on acquisition to the company I'm running today—a gentleman sold his company for $16 million. He had $2.5 million in earnings at the time. He rolled over $4 million, and took $12 million home and stuck it in the bank. (Obviously, he paid his taxes.) Twenty-seven months later I sold the company I'm running from one private equity group to another, and we got a 4x return on investment, which means his $4 million rollover investment returned $16 million in 27 months. If you recall when he sold his business the first time, he sold it for $16 million. If he would've said "one-and-done," he would've ridden off into the sunset with his $16 million and that would have been the end. However, he rolled $4 million forward and took $12 million home, and that $4 million became $16 million in 27 months. So in total $32 million minus that $4 million rollover that he did—that was already his money—so in essence he got paid $28 million.

He had so much fun, he went off and bought a winery in Napa, but he rolled forward again. He rolled forward $5 million more that is currently invested in the company today, looking for now his third bite at the apple.

So what I wanted to be sure to educate people about, especially business owners, was that they shouldn't think of selling a company as a one-time event. They should think of it as an opportunity to take some money off the table while at the same time being invested in this new partnership with private equity. Continue to run the business and be aggressive, make good business decisions, but not risking the family farm, if you will. Or betting the farm because they now have liquidity outside. Then in doing so getting a chance to do a second bite at the apple.

My personal record is five multimillion dollar paydays across a 13-year, four-month period running a company. I've been at this company for 3 1/2 years now and some investors have already seen two bites of the apple, and we're working on that third. To me that's the most powerful message in the book, for people out there to not think about selling a business as a one-time event. It's not just about who puts the highest price on the table. It's about who can be the best partner to give me an opportunity to not just get one bite but two bites or three bites over a relatively short period of time.

MN
So the title of our new e-publication is "Thrive Through Data." Looking at CoolSys, in what ways does that describe your work that you do there?

AC
I've worked in service businesses for 35 years. I've been running them for 20. I have an engineering background which makes me kind of a tech nerd to begin with. What I've learned is that if you can't store your company's product in a box, then your product must be people. In service businesses like CoolSys, your product is not refrigeration or HV/AC. Its people. If I invest in culture and people, I get an engaged workforce. That engaged workforce takes care customers. Customers give me more stuff, and revenue rains from the sky.

But in order to build an efficient service business, I have to rely on data. So I invest heavily in technology in any company that I'm running because I find that technology and data allow us to make the workforce much more productive in a service environment. Can I get the right person, with the right part, in the right place, at the right time? That's really a function of analytics and data. So I've worked with companies like Blue Margin using tools like BI365 to create data lakes to collect every bit of information.

I have 2,800 employees, and in our world there's 1,900 people in trucks out there driving around right now. If you think about how many service calls that workforce can complete in a year, or two years, or three years—by capturing all the data related to failures and model numbers and parts used, and diagnosis errors reported, and fixes, and all of those different aspects, you can truly then use data to transform a company to drive what I'll call predictive analytics, business intelligence, and machine learning.

You can wind up growing exponentially faster, organically. Servicing more customers, taking more service calls, doing more things, regardless of what the company is. I can make my workforce more productive, so I'm still adding jobs. I'm still adding people, but by making them more productive, I'm able to leverage the organic growth, or the merger-and-acquisition-acquired growth in a much more efficient manner.

I think in the last company that I ran full stop, when I had started and finished with that business. we improved productivity in the field by more than 42% by investing in technology, by using data analytics, and using that to inform our decision-making process. Real-time, on-the-fly, live to be much more efficient. So imagine if your workforce out there was 42% more efficient today, how much more customers could you serve? How much more activity or widgets could you make, regardless of whatever the company does?

So to me, investing in technology drives employee productivity. It takes data that's collected and data that is analyzed in order to keep that engine going into the future, to help you make better business decisions about how you're going to utilize your workforce.

MN
Now correct me if I'm wrong. When you, at CoolSys, make people your priority, that also spreads out into making charitable efforts a priority for your company? Is that correct?

AC
It is. CoolSys, as a company, has its own internal foundation that was set up by our owners. And is also funded by employees and by the business. The same tools and things that you learn building data-enabled company not only can make you more productive, but then also provide you with data and insight into other things.

We have a strong effort around keeping a pulse on our employees’ engagement and are constantly asking for their input and their opinions on different matters that are occurring in the world today. As a result, we're collecting data there too, and then using data to inform how we think about employees. Not just employees but benefits. In today's world, being a conscious employer of the world around you is also an important facet of keeping employees engaged and keeping employees working at the company.

So data touches everything that we do. In some cases, it's enabling productivity internally. In other cases, it’s helping us analyze the employee experience. That then also parlays to our customers, trying to provide a better customer experience and to be more of a trusted partner and less of a break/fix service company.

MN
That's good. Now tell me a little bit more about that foundation.

AC
So we just recently set it up. It's the CoolSys Foundation. Our first recipients were employees. Any employees who were impacted by COVID.

CoolSys is growing. You know, we have different types of business. One of the areas of our business that was impacted by COVID was construction. A lot of our customers were delaying construction projects, delaying capital projects and some of our employees were impacted or furloughed as a result of that. So the first thing that the CoolSys Foundation did was to make grants available to employees who had been impacted. So between the state unemployment, the federal enhancements, and the CoolSys Foundation, the goal and objective was to make sure that our employees that were furloughed did not suffer any severe economic consequences as a result until we could call them back. At one point out of 2800 employees, I had about 194 on furlough. I think this morning my report had us in the 20s. The majority of people who are still on furlough today would be people who have preexisting conditions, or they're elderly, or they're just people who are not comfortable coming back to work right now.

So that's an example. As we turn and head into the fall, that foundation then will be helpful to employees who are impacted in multiple ways. Whether it's a medical emergency, a family emergency, a hurricane, impact through things like that. The foundation right now, its primary focus is internally to our employees and our employee families

The company as a separate entity continues to be active as well. From a philanthropic perspective, in the community, there are a number of different charities that we have made commitments to in Orange County where we're headquartered, including Children's Hospital of Orange County (CHOC). Then also the Orange County Rescue Mission, which is a homeless shelter that tries to help homeless people actually transition back to productive members of society by providing job training, healthcare, wardrobe, food, a place to live. It's almost like going to college. So there's a number of charities that we have helped support in the community.

I think when you take all of those in combination, it speaks to who we are and what we think. A culture reflects the values of the CEO to some degree, I've been a successful guy across my career. I don't compromise my personal beliefs on culture and on the importance of taking care of employees and the broader community for the sake of shareholders or profit. I've spent 20 years perfecting the idea that you can be both successful in building a strong culture, taking care of employees, being a productive member of the community, and then at the same time, also service shareholders and give them outsized returns. My ultimate goal and objective is to do both

MN
Nice. So you guys are in Brea?

AC
We're headquartered in Brea. We have 74 offices across the US. Brea is our headquarters.

MN
I worked my way through college selling jewelry at Brea Mall up there.

AC
Right across the street. Literally.

MN
All right. I want to take us back to your book for just a minute. I found your chapter on EBITDA fascinating. Can you give us a little bit of your perspective on that?

AC
Yeah. In a public company it's all about earnings, price to earnings. In the private world non-institutionally held private world, most people who found businesses think about company finances in terms of cash. What's my cash profit? Am I burning cash, am I building cash?

EBITDA is a line that most private company, founder-owned businesses just aren't really focused on. In the private equity world during a three to five year hold period, there's going to be a lot of investment in a company. So if you think about earnings before interest, taxes and amortization, you have to figure out at what level in the P&L, in the balance sheet, and the statements, do you value a company from? Private equity tends to use the EBITDA line, and EBITDA for some people is just a foreign term that they're not familiar with. So they think differently.

I'll give you an example that I like to use. Let's assume a company has a fleet of vehicles and they decide to buy those vehicles outright because they don't want to have monthly payments and so they make 100% capital expenditure. By doing that, in a privately-held company environment, it's a capital investment. Capital investment is below the EBITDA line, so it doesn't impact my earnings. If I'm being measured as a multiple of EBITDA, and that's going to determine my purchase price, I'm far better off to expand the cash capital and buy my vehicles than I am to lease them. If I lease those vehicles, then they hit my operating P&L. If they hit my operating P&L, I don't expend as much cash, but I lower my EBITDA earnings. So for a small business owner who is thinking about their business in terms of cash, then they may be making decisions about equipment and about policies and procedures that allow them to hold more cash and lower their taxable earnings.

So if you're a small business owner, you think about it in terms of, how do I minimize my tax payments? If you're a privately-held company, in a leveraged buyout scenario, you get to deduct interest that you're paying on debt from earnings. Most private-equity-backed companies are not cash taxpayers. They're not taxpayers. They're investing heavily in a company because they want to grow it fast. So in a given period over the next three or four years, I'll spend $800 million buying companies. When I think about that kind of investment, there's no way possible that the company could generate enough free cash flow or enough earnings to allow me to use all cash. So there's a heavy debt component there,

If you think about it in terms of cash, or like a public company price to earnings, most private equity backed companies would have negative cash flow. They would have negative earnings, and it would be almost impossible to value the company. So a company that is investing has less cash earnings. In the private equity world, your goal and objective is to double, triple, quadruple the company over a 3 to 7-year period—call it on average 5. So EBITDA is a strange new concept

You have to understand the difference between how it was when you ran your business, when you were an independent owner/operator or a founder-owned business, versus once you're institutionally held. You have to reprogram yourself. You've been thinking all along. "It's all about cash in the bank, so do whatever you can to conserve cash." Leasing things is OK and you're very, very focused on cash flow. In a private world you're using credit, you're using credit lines. You're investing. Anytime you're investing, cash earnings are going to be low or nonexistent. So in order to value a company the private equity world uses a multiple of EBITDA. Rarely is it based on a price to earnings, public type component that most people would be familiar with.

If you have an E-trade account and you're buying mutual funds or stocks, you're looking at price to earnings ratios, and you know that different sectors like tech have really high PDEs, and utilities are low, but they pay good dividends. So you have to just kind of really rethink everything you've ever learned about finance, and reprogram yourself to understand, "What is EBITDA and how do I maximize it?" How do I focus not on cash but focus on EBITDA generation so that when it's time to exit the business I have a higher valuation?

MN
Alright, we're moving into The Dirty dozen so the rules are whatever comes to mind first. We're going to go through 12 questions in the next 3-4 minutes and there are no wrong answers. Are you ready?

AC
I'm ready and is this a one-word answer or is this give you my thought?

MN
Give your thought whatever it requires. So for instance, the first question is: What were your nicknames when you were a kid?

AC
I can't even tell you the why. When I was in the military, I was a skinny kid. I was like 6 feet tall, 120 pounds soaking wet and so people called me Sticks. Another group of people called me Sergeant Leroy. I have no idea where that came from. I played basketball, so people called me Swish for a while because I was an outside point guard who was a shooter and the perfect shot for me is nothing but net. So I've had a lot of nicknames over the years. None of them any good, by the way.

MN
So you know, if I ever meet you in person, I'm going to come up and say Hey sticks, how's it going? Where were you born?

AC
Chicago IL

MN
What's Next up on your Netflix watch list?

AC
Netflix watch list. Right now I'm binge watching Dexter. I'm somewhere in season five. So I'm going to say probably Dexter. You know, continue that binge watching.

MN
Best book you've read in the past year?

AC
Best book I've read in the past year. Boy, I can't say my own. because I read that thing 500 times. I'm kind of an old school guy. So I mentioned in my book a book by Sandy Ogg, a called Move. Sandy, worked at Blackstone and he really revolutionized how private equity firms think about human capital, and building management teams, and driving outsized performance. So I'm going to go with Sandy Ogg, his first book called Move, which is the CEO's guide to managing people. He has a second book [Grow] that just came out which I do have, but have not yet read.

MN
Good. A hidden talent. The thing you can do that nobody knows.

AC
All right. Let's see. I can play the drums. I can roller skate. I started playing hockey when I learned how to walk. So I was on skates at like 3 years old. Not that that's much of a hidden talent, but hey.

MN
And I hear you can swish a basketball, right?

AC
Yeah, Yeah, but I'm getting old now.

MN
What's the thing you can't do to save your life?

AC
I can't play golf to save my life. I'm a jock. I was a pitcher in baseball. I was a point guard in basketball. I was a goalie in hockey. I mean I was a big sports nut growing up. There were only five channels on TV. There was no video games at the time. Cable TV with 1000 channels didn't exist yet. There was no Internet. So we played sports. Golf is a sport where if it's a scramble and I go out and I play, I'll get a good shot here there. But I can't break 100 to save my life. So I just stopped playing. I just I blamed it on my shoulder. Bursitis is acting up.

MN
Favorite sports team?

AC
Anything, Detroit. Detroit Tigers, Detroit Lions. I'm 56 years old. My entire life I've only seen the Detroit Lions win one playoff game.

MN
Oh my, that was Barry Sanders, right?

AC
Yes. They beat Dallas. They lost to the Redskins. I remember that. They've won one playoff game my entire life, but like a true Lions fan, I watch every game. Even the 0-16 season. It was a badge of Honor. And so you start anew every year.

MN
I have new respect for you. Adam. New respect. Alright, best gift you've ever received?

AC
Best gift I've ever received. You know I'm going to go back a long time to my first computer. My wife got it from an insurance auction. I wasn't a wealthy guy back then, obviously. I was struggling engineer. My wife got a used Apple Mac SE, I think it was. It was my first computer. That's going back a long ways now. That’s probably the best gift I ever received. I could say something sappy, like my daughter, my son, but if I think about just a practical gift, I'd say it was the first computer.

MN
Worst advice anybody ever gave you?

AC
I'm going to go to a resume. The worst advice I ever got was trying to comply with a resume service trying to make you into the quintessential, generic human being. You know, where your resume would never stand out in a crowd. I was the kind of guy who would want to put a picture on the resume, who'd want to put some factoids that mean nothing. I was soldier of the year in 1984, and I remember when I got out of the service a resume service that was provided by the government at the time, said “Nobody cares about that.” At the end of the day, when I got hired, my first job coming out of the service, I had none of the skills and none of the qualifications for which the job was looking. But the hiring manager was an army captain and he said, “You know what? I know what it means to be soldier of the year. And I know you'll show up to work on time. We'll figure out the rest, but I gotta have you.” So worst advice ever was listen to a resume service about what your resume should look like.

MN
What did you like best about being a student at UCLA.

AC
The learning! I had what I would call it a good academic grounding, growing up. I went to private school, a mixture of private and public school. I think what UCLA taught me at the time that I went, which was not early in my career, it was that I had a lot of raw talent, but perhaps not a lot of academic understanding. So I don't want to call it dumb luck. I was doing things well in my career, but I wasn't necessarily doing them with consciousness, or conscious thought about what I was doing. What UCLA certainly gave me was, you know, call it academic excellence and an understanding of the different processes and things that I was doing.

I think probably the most useful thing I learned about in Business School was about blue ocean and the idea of taking a company and making it pivot in order to find blue ocean. Blue ocean is free of competition. Red ocean is red from the blood of competition. It's taking an old stodgy company that is in a slow-growth area or in a commoditized area and doing just a little strategic pivot to find blue ocean. Then finding opportunities for rapid growth and advancement where perhaps the company wasn't growing for some long historical period of time. The company I'm running today, we have a 27% compound annual growth rate. I buy a company. It grows on average 25 to 30% within the first year after we acquire it. Doing strategic pivots to find all these new verticals, adjacent verticals—finding that blue ocean was a real impactful thing. That was probably the most valuable lesson I learned. It formalized what I was doing, taught me the process and the academic reasons behind it, and it made me a better leader.

MN
Nice, alright. Last question. Favorite thing to do in your spare time?

AC

Go for a bike ride with my daughter. I just got this cool new Rad Power Ebike, a fat tire Ebike. I am an old guy so I go on trails and going up hills is just not what it used to be. But it lets me keep up with my seven-year-old daughter who is just an absolute rocket. She weighs 50 pounds nothing, and there's no hill she can't conquer or no trail she can't ride. So that was my favorite new COVID toy to get me out of the house. My new Rad Power fat tire Ebike. I think they call it the RadRover

MN
Well Sticks, it's been great talking to you. I appreciate you taking the time. I will send you an email when this posts. This will probably go up in October.

AC
Sounds great. Thank you for your interest and thank you to your listeners. Hopefully I didn't bore too many people.

MN
No, you're awesome.

AC
OK, take care.

MN
Thank you very much. Bye bye.

AC
Bye bye.

[END TRANSCRIPT]