Tim Lyne

Episode 230: The Convergence of Insurers and Asset Managers

GUEST Q & A

Stewart: Welcome to another edition of the InsuranceAUM.com podcast. I'm Stewart Foley. I'll be your host. We've got, I'm very excited. I can barely contain my excitement today to have Tim Lyne on. Tim Lyne is a founder of a company called Antares Capital. And as a founder of a company that is substantially smaller, I feel a little bit like we're kindred spirits in the founding of a company. And so we're very excited to have you on. Tim, thanks for taking the time, and thanks for joining us.

Tim: Thank you so much for asking me to join. Excited to be here, Stewart.

Stewart: Yeah, it's good. So you are the CEO of Antares Capital and as I mentioned at the top, you were one of the founding partners of Antares Capital. Your story goes back into the 90's and I want our audience to really come away with a sense of you and how all that happened because there are very few firms that I would have the chance to meet someone who actually was a founder. So, I'm super excited about that, but I got to run you through the same gauntlet that I put everybody else through. So here we go. What town did you grow up in? What was your first job? Not the fancy one. And what makes insurance asset management so cool?

Tim: So Stewart, I grew up in Chicago. That's unusual because many people will say they grew up in the suburbs, but I grew up in the south side of Chicago in an area called Beverly. That's where I had my first job as a paperboy. So I had a paper route and delivered the afternoon paper. They don't have that anymore, but I delivered the afternoon paper after school. Then my first summer job was as a camp counselor.

Why is asset management so cool? I would say it's because it's very complex. What I mean by that is allocators at insurance companies need to navigate complexity in their asset allocation and complexity in implementing the proper vehicles that provide capital relief. So when you think about asset allocation, those insurance allocators need to do more than just target a specific return profile at the portfolio level. They also need to analyze the assets and liabilities to determine the proper asset allocation, and they also need to consider the evolving regulatory environment - and structure their investments to maximize the return profile of the portfolio.

So as you know well, and your audience knows well, if you were to invest or they were to invest in a senior private debt fund and/or a private equity fund, they would receive the same 30% capital charge. But by structuring the private debt fund properly, and we can help them with that, they can significantly reduce the capital charge. And obviously that benefits them from a return standpoint. So I have significant respect for allocators in the insurance space because it requires very sophisticated investors to navigate that complexity.

Stewart: You're helping me up on my soapbox when I start talking about how insurance asset management is the most sophisticated asset management in the world, and it's because of the externalities that you're referring to. I mean, in one-dimensional world, in other institutional markets, you're focused on return, but in the insurance space, there's so many other things going on. But I want to go back to where I started at the top, which is you founded Antares back in the 90's. Can you talk about how it started? And you obviously have become incredibly successful, but were you scared to death when you started it like I was, and still am, frankly?

Tim: So I'll give you the story. There were 12 of us – so the 12 founders were working together at Heller Financial in 1996. Heller was a large commercial finance company headquartered in Chicago. We were focused on providing financing to private equity sponsors in the Midwest for acquisitions. So similar to what we're doing today, but we were part of this much larger company.

So a guy by the name of Barry Shear, who was one of the founders, had this idea of starting our own company. And there would be a couple things that would be really unique that we thought would be a big draw to the sponsors. So one would be 'hey, we'll find someone…a major capital backer…where we can own the company with them. And I think the sponsors will find that really interesting.' So that was number one. The other was 'let's have our team comprise the investment committee'. So we will be making the decisions on the companies, which companies we finance versus which companies we turned down. And by having that in-house, it should be a major value prop to the private equity sponsors because we should be much more responsive than our competitors because when we started, there were 12 of us. And so deals would come in and we could call an investment committee meeting at any time of the day, at any time in the evening, call committee meetings on weekends, on holidays.

Even though I'd say many more companies are able to do that today, when we started, that's not how our competitors worked. It was that you needed to send a deal out a week before you went for approval. And so ultimately, we all thought it was a great idea. We thought it would be really hard to find the money. Barry had a close friend, a very wealthy friend named Shel Lubar out of Milwaukee, Wisconsin, and he ran the idea by Shel to see if Shel would be interested in personally investing. Turned out that Shel said, "Hey, I would be interested, but more importantly, I'm on the board of MassMutual and I think this is something that MassMutual would love, so let me make the introduction." And four weeks later, MassMutual had full approval and backed us with a billion dollars to start the business. So that's kind of how it started.

When your question about was I really scared about it. It's interesting. When I ran the idea by my mother, she was like, "Huh, I don't know why you would do that." My parents were both educators, but I did run the idea by two of my aunts who were very successful businesswomen. They were like, "of course you should do it. If it doesn't, you're 30 years old, you're married, no kids. If there's ever a time to do it, it sounds like you have a great business plan. Now's the time to take that risk." And so, were we a little bit nervous? I think we were some more than I because others had children. And so that made it a little more worrisome for them. But started the company and it was really exciting. We had to find office space, we had to find, back then we had to find phones. And back then it was the landlines.

Stewart: And it was expensive. It was expensive. Those turret phone systems are expensive.

Tim: Yes! And then we started traveling. So I was given the West Coast to cover. And luckily for me, there were a lot of private equity groups that started, were founded in the mid to late 90's in California, in particular in San Francisco. And we still do a lot of business with those groups today. But again, when we started telling the story, it really resonated with the private equity sponsors because they were like, "wait, so you guys, you're backed by this major insurance company. We love that. So significant capital, you own the company with them, you're making the credit decisions." And so that part was great. And the other thing that we really stressed to them was reliability. So we told them…they would send us a deal, we might call them back the same day or the next day with a turndown. And I think they were a little bit surprised, like, wow, it didn't seem like you spent a lot of time on it.

But our point was, "Hey, we're going to be really reliable." On deals that we know that we're not willing to underwrite, we'll let you know that very quickly. And on the deals that we really like, we'll provide feedback very quickly on what we think the structure and the pricing of that deal should be. We'll also send you a list of diligence questions where we're concerned from a diligence standpoint and how we intend to mitigate that during due diligence. But importantly, the idea was if the due diligence proves out, which usually it does, we'll be there for you, we're not going to change the terms of the deal. So what we tell you upfront, we're going to get there on that unless there's adverse due diligence findings. So once we started closing deals with some of those sponsors, it worked really well. They enjoyed working with us, we enjoyed working with them. And I think for them it was kind of a new process. They were like, wow, that was so easy. It was so quick. And we started to develop a lot of trust between the groups.

Stewart: That's really cool. And I really sincerely want to give a shout-out to the folks at MassMutual. It's another way that insurance companies don't get credit for their innovative practices. So when you talk about bringing an asset management firm to market like Antares like they did or were instrumental in, it's fostered a lot of growth and a lot of financing deals along the way. I mean, I've always got a chip on my shoulder where the industry's concerned. I feel like I need to defend the industry for some reason. And I just think there's a lot of good that insurance capital has done for a lot of businesses. So when you founded back in the late 90's, who were you competing with back then for those early 2000's deals? There's a significant number of direct lenders. Today this market looks very different. What was the landscape like at that time?

Tim: Yeah, very, very different from what you see today, Stewart. So, I think today they say there's over 2000 direct lenders. That terminology didn't exist. Direct lender, private credit, private debt, none of those terms were used. We were really competing mostly with regional banks. So, some of the names would be Fleet, Bank Boston, KeyBank, LaSalle Bank, First Chicago, to a smaller extent. Interestingly, the French banks were quite aggressive during that timeframe and in several of them. So, BNP, Crédit Agricole, and Indosuez Capital would be names that were certainly aggressive in that late 90's, early 2000's.

Stewart: Very interesting. And so how has the direct lending market evolved over time? So obviously with 2000 plus direct lenders today, I think a corresponding significant increase in the acceptance of this asset class by insurance companies in particular, because I kind of get on my soapbox a little bit here too, but when you think about banks lending, the nature of their liabilities and assets don't really line up particularly well, which is why the FDIC backstops them. But in insurance land, it makes a lot of sense because there's a very nice hedge, almost, that is consistent with the nature of the insurance liability. So talk to us about that evolution.

Tim: So it's pretty amazing if you look at the growth in the direct lending market and how it has evolved over time. I'll start with the banks. The banks have continued to exit the financing markets, sponsor financing market over the last 20 years. So I mentioned a number of those banks that I mentioned a while ago, they're really not in the business anymore. Each time there's an economic downturn, it seems like more of them exit the sponsor financing business, and that then pushes more of the financing to the direct lenders. Another thing that's happened with the private equity sponsors is many of them, we would say certainly over 50% of our tier one and tier two sponsors, now have capital markets professionals within the firm.

So, if you go back 20 years ago, you had the different partners at the firm and they did both the diligence and the financing. And then that started to change with the idea that you would have the partners that focus on the diligence with the teams, and then you would have other partners or team that focuses on just financing. So let's create a specialized financing group within the private equity sponsor. In many cases, those financing professionals within the sponsors have focused more on the private credit market than the syndicated market.

So, I think what they have done, many of them over time, is developed relationships with 3 to 7 or 8, some cases more private credit lenders, and they kind of go to them on their deals. And certainly, they will sometimes also on large, large deals, maybe also look at a syndicated option. But the idea is if you compare the syndicated deal to the private credit deal, the syndicated deal is going to require ratings. So S&P and Moody's need to rate the deals. In many cases, it's going to require a syndication process. So management needs to get up and kind of tell their story. The books may go out to 50, 100 or more players, so some worry about confidentiality, but in general, that process might take 6 to 8 weeks. Private credit, there's no ratings that are needed. There's not a true syndication process, and importantly there's not flex. So, the syndicated deal has pricing flex so if the deal's not selling well, you can increase the pricing. Similarly, if it's selling really well, the pricing could decrease. But the private credit deal, it's kind of 'here's the structure, here's the price'. There's not that flex 95% of the time. So more and more sponsors started to gravitate to the private credit option. So that's why you've seen the significant growth over time. The banks retrenching.

Oh, actually I'd add one other thing, Stewart. It's just the overall growth. There's fewer public companies, so more companies are owned by private equity sponsors today than 10 years ago and 15 years ago. McKinsey says they think it's maybe 12%, 13% of middle market companies in the US are owned by private equity sponsors. And that percentage is expected to increase. So if you just think, okay, here's how it's evolved over time, and if I fast forward, if more companies are owned by private equity and more private equity firms use private credit as their option, that's why the industry's projected to grow 15% to 20% a year for the next 5 years.

Stewart: That's really helpful. So what I've seen is many of the larger private credit platforms moving up market over time and lending to companies with higher levels of EBITDA. Has this been your experience as well? And what can you talk to us about that?

Tim: So Antares has not made a strategic decision to move upmarket. Historically, the firm was founded with a focus on the middle market. The definition of the middle market has probably changed a bit over time. Some folks say $15 to $20 million in EBITDA on the small side, up to $75 to a $100 million on the large side. And beyond that, beyond $100 million maybe becomes the upper middle market. So major focus on the middle market, but we will go where we see value. So when there was dislocation in the upper middle market where pricing moves quicker than the core middle market, we might play a bit in that upper middle market, but we've not made a strategic decision to move upmarket.

What's happened though is if you look at the median and average EBITDA in our portfolio, the median EBITDA is around 60, average EBITDA is in the mid 90’s. Those have both increased over time. And the reason they've increased is because there's many sponsor-to-sponsor sales, and sponsors tend to be acquisitive. So there are many companies in our portfolio that have been in the portfolio for 10 or 12 or 15 years, but they're on sponsor number 3 or 4. So we financed it when it was $20, that sponsor grew it to $40, sold to another sponsor that grew it to 70 and now it's $100, and it stayed in our portfolio each one of those times. So that leads to kind of the average and median EBITDA increasing. Others, some of our competitors that might be defined as more asset gatherers have strategically decided to move upmarket. And I get it, if you have raised vast amounts of capital, are you really going to focus on $50 and $75 and $100 million dollars EBITDA businesses? Or are you going to try and go win the ones that are $300 and $400 plus in EBITDA?

Stewart: And when you talk about financing a company in various stages of their growth, that really speaks to your earlier point about Antares being reliable, right? I mean, that's over a number of years that you're with the same group and they come back to you, you do business with them again, and those relationships, it matters. It differentiates your deal flow, I would think.

Tim: Absolutely. It's critical. So I would say it's one of our biggest differentiating factors or competitive advantages is that we've been working with many of these sponsors since the sponsor was founded, whether that was 15, 20 or 25 years ago. And in many cases they've only during that time had one or two sponsor coverage professionals from Antares. So, our sponsor coverage people are very experienced, all grew up in credit, have been here a long time, and so they kind of have those points of contact. I mean, there was a group of us that had dinner just last night with a sponsor. We have over a 20-year relationship with them. We were saying at dinner just since the CPP acquisition, we have financed over 100 transactions for them. And as you know Stewart, they don't all go well. So one of the conversations we had last night was the fact that yes, we can be tough when deals don't go well, but we're also constructive. So there's no free pass. So if we are going to PIK some of our interest or defer some amortization, we're only going to do that if the sponsor is willing to support the company as well with additional equity or capital call or something like that. So that even further strengthens the relationship when you go through tough times and you've worked through multiple economic cycles in the past.

Stewart: You mentioned CPP, which stands for Canadian Pension Plan. It's interesting, they, I believe, own a couple of insurance companies as well. What's your relationship with your owner, CPP, and how has their insurance company ownership been a part of that?

Tim: So yeah, we have a very strong working relationship with CPP. And so for folks that'll be listening to the podcast, Canadian Pension Plan is one of the largest pensions in the world, managing over $500 billion on behalf of Canadian pensioners. They purchased the company in 2015. They're the majority owner of the business today. So it was really interesting when we were being sold by GE, it was mostly competitors that were part of the bidding process. CPP had written a white paper on the North American sponsor direct lending market, and that they were going to try and attack that market organically. They felt like there was a huge opportunity in that space and that market was going to grow significantly.

And all of a sudden Antares was available for sale and they're like, “wait. Lot smarter here to buy versus build.” So they understand. They work with sponsors as well. They have a very large debt business. We have great governance. There are 3 CPP members on our US board along with 3 independents and me. They do have insurance companies. And those insurance companies have been very helpful to Antares. So those sister companies provide us with unique insights into building our insurance solutions. We also exchange notes on the regulatory environment. Just about 2 weeks ago, several Antares colleagues and I met with the senior management team from one of those sister companies to discuss some options for structuring some insurance-friendly vehicles. So it's worked quite well.

Stewart: That's terrific. So I'm wondering if the trends in M&A have come up in your conversations with your sister companies. There seems to be a convergence in asset managers and insurance companies. There's been a deal announced in the market recently in the last couple of days. As the founder of Antares, what are your thoughts on this trend?

Tim: So I'll start by saying it's a really exciting time for Antares, and then I'll kind of roll into the insurance side. So we have numerous growth options that we're currently pursuing and there are others that we plan to pursue kind of in the next 2 to 3 years. We've experienced significant growth in managing capital outside of our balance sheet. So if you think about the business under MassMutual and under GE, so for the first 20 years of Antares, we were essentially a proprietary shop managing capital on behalf of our owner. And that was what the original plan was with CPP. But we really have started managing a lot of capital outside of our balance sheet.

So given that strong growth, we also see numerous M&A opportunities. It certainly helps too, that we're backed by one of the largest pensions in the world that's very well known. And we actually believe there's a pretty symbiotic relationship between insurance companies and asset managers. And that's why you've seen some of these transactions like the Kuvare one that was just recently announced, there was the Global Atlantic one that's been around for a while. So when you think about it from the insurer's perspective, these deals provide capital to the insurer so they can then grow their book of liabilities.

From the asset manager's perspective, you not only earn a return on the investment, but you’re also taking capital and then you earn a fee on that capital. So, I think these insurance investors are building these relationships with managers that complement them as they also build their own in-house investment programs. So, we're reviewing numerous opportunities, even right now, to partner with insurance companies in some strategic capacity. And we really don't look at these M&A opportunities as a trade or simply a way to raise assets. We are really looking for long-term strategic partnerships, but because they're long-term strategic partners, it's really important to us that we are aligned with the insurance company's management team regarding their long-term vision of how they intend to grow their business.

Stewart: That's really interesting. And just sort of to follow up on that, what has been Antares’ approach to building your insurance business?

Tim: If you think back, I kind of think of our legacy is really insurance because we were backed and owned by a very large life insurer, MassMutual, and they founded Antares with the management team in 1996. And I don't think of us as asset gatherers. We've been very deliberate in our approach to the insurance market. In addition to the traditional fundraising that you would have with insurance companies, we're building strategic relationships. That would include things like supporting capital raises, co-investing relationships, providing exposure to our CLO business, which is industry-leading. In some of those opportunities, it allows the investor to participate with GP economics. And what we've done is we've built a sophisticated team of insurance pros who work with our structuring group to really build these capital-efficient solutions for the insurance companies. That would include things like rated feeders, rated notes, CLOs, SVO rated funds. And we know that each insurer is unique and they operate under different sets of constraints. So the idea is to work closely with them to develop innovative and personalized solutions to optimize their capital efficiency.

Stewart: We've talked a lot about insurance and Antares, and how they fit together. Can you talk a little bit about where you think there are competitive advantages that you would call out given where you are today and where you see the opportunities going forward?

Tim: Sure. Stewart, I'd hit on 3 topics. One is let's just begin with the alignment we have with our investors. So we have this $25 billion plus balance sheet, and we're taking significant hold positions on every deal we close. So therefore, we are very aligned with our investors because we're looking to protect their capital as well as our own capital. And I believe that that's more impactful than a 1% to 3% GP commitment to a fund.

Second thing would just be the breadth of the portfolio. So many of our peers, when they're building a portfolio for their investor, it might be comprised of 50 to 100 borrowers. Ours is typically going to have more borrowers. So it's going back to that breadth and depth of the sponsor relationships. We see almost every deal in the middle market. We're highly selective and only close about 4% of them. But when you put that together for the investors, it means we can deploy, given that volume, we can deploy capital quickly and build a highly diversified and defensive portfolio for all of our clients, including insurance clients. But for the insurance clients, that diversity should really help them with a favorable nod from the rating agencies.

And then the third thing would be our workout team. We call it our credit advisory team. It's 15 individuals, 5 people that are very senior managing directors and above, and they get involved very early on credits where we are seeing some stress. And it really allows us to minimize losses. And as you know, that's really how you create alpha is by minimizing losses in our portfolio. And that credit advisory team is instrumental in helping us accomplish that.

Stewart: That's really helpful and I appreciate it. I've gotten a really terrific education today and I really appreciate that. I've got a couple of fun ones for you out the door with some optionality. You can answer any or all of these. What is a fun fact about Tim Lyne? And secondly, what is a great piece of advice that you've gotten along the way that you'd care to pass along? And last but not least, if you could have lunch with anyone you chose alive or dead, who would it be?

Tim: No, I like it. Fun fact about Tim Lyne, I met my wife, Mary, on a blind date. I feel incredibly fortunate. I'm very thankful to a woman by the name of Sheila Weimer, who I worked with back at Heller Financial. She had the idea to set us up. She and her husband didn't go with us on our first date, so it was truly a blind date. And we've been married for 28 years, so that's a pretty cool, fun fact.

Stewart: That is a fun fact and congratulations. That's awesome.

Tim: Thank you. Best piece of advice, or one of the best would say, I always say “Never rest on your laurels.” We always need to be evolving, moving, innovating, and if we're not, others are going to catch up or they're going to pass us. I also tell my team all the time, “Change is inevitable. Growth is an option.” So, we really need to be receptive to change because change happens all the time. And that if we have a positive mental attitude, we're going to be much more receptive to change. So those are the biggies. I mean, at the end of the day, what's so important is we always have to act with the highest integrity, treat everyone with respect. To me, those are givens.

If I could meet one person, it's not going to be someone famous. It's actually I would say it would be my late grandfather. If I had the opportunity, there are so many different questions I would ask him. His name was Tom Lyne, so he was my father's father. Immigrated to the US from Ireland when he was 19 years old, did not even finish high school in Ireland. That said, we believe he was absolutely brilliant. He worked a blue collar job. He and my grandmother had three children. So again, she also did not finish high school. Their three kids, two of them earned master's degrees, one earned a doctorate. Education was hugely important to them. He was a voracious reader, and it was all about history, labor movements, politics. And I remember him wanting me to read The Jungle by Upton Sinclair when I was in seventh grade, and he wanted to discuss it. So once again, kind of this intellectual who was a blue collar worker and an immigrant. I blew him off. I never read it. And truly, I look back at that now and I kind of regret it. So, I would love to meet with him and kind of say, “Hey, you were one of 11, you had 10 siblings, you had parents and you left on your own to come to the US. How did you have the courage to do that? Why did you stop in Canada? How did you end up in Chicago?” And it was just really, he had a passion for human rights, big proponent of unions, and he had this passion for the US because of all the opportunities that were offered in America. So, you never heard him complain because I think he was just so excited to be living his life in the US. So that would be it, Stewart.

Stewart: That's fantastic. Thanks so much. We've been joined today by Tim Lyne, CEO of Antares Capital. Tim, it's been a pleasure. Thank you so much. You grew up in Beverly, which is people who know Chicago well…. there’s a strong Irish presence and strong Irish traditions in Beverly to this day. And it's a wonderful, wonderful neighborhood in Chicago, and I'm sure you're proud of your heritage, there.

Tim: Absolutely. Thank you for having me, Stewart.

Stewart: My pleasure. Thanks for listening. If you have ideas for podcasts, please shoot me a note at Stewart@insuranceaum.com. My name's Stewart Foley. This is the InsuranceAUM.com podcast.