*From left to right, the leadership team at U.S. Capital Advisors: David King, managing partner; Rebecca (Becca) Followill, senior managing director and head of research; Michael McConnell, managing director for merchant banking; Patrick Mendenhall, managing partner; and William (Bill) Hurt, senior managing director for investment banking.* Source: U.S. Capital Advisors

# Generating Capital

**Led by a team of industry veterans, the breakaway Texas investment firm U.S. Capital Advisors LLC is powering up.**

**By Deon Daugherty,** Associate Editor

Before super-sized master limited partnerships (MLPs) became giants in the energy industry and the MLP-focused Alerian Index emerged as a go-to for investors, David King was plugging away at UBS and Deutsche Bank with an eye trained on the midstream asset class. That was also before the financial crisis left many brokers disillusioned when large banks retrenched.

King's UBS colleague, Patrick Mendenhall, led the wealth management side, and both men were interested in doing something different.

"You had some very talented people who were looking for other opportunities," King tells *Midstream Business.* "They and their clients did not have a good experience during the financial crisis and were looking potentially to do something more entrepreneurial. We saw the ability to form a firm that wasn't just an energy boutique or a wealth management firm but to build a regional, diversified financial services firm."

In late 2010, King and Mendenhall founded the capital investment and wealth management firm in Houston with two equity rounds worth $18 million from high-net worth and family-office private investors. The pair has subsequently plucked staff from the majority of the large global investment banks as well as a number of energy-focused regional firms, with an approach that relationships are key and long-term, stable growth is an incentive.

Investing in finding the right team has paid off in dividends. U.S. Capital has grown from a handful of employees to more than 80 dispersed among three offices across Texas. Current assets under management total $2.6 billion,

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a figure that King expects to increase as the firm attracts new wealth management teams.

The firm's capital markets business is focused solely on energy and energy infrastructure with a significant focus on MLPs.

"We were working with some of the first MLP-dedicated institutional investors back in 2003, 2004, and we still work with them today," King says. "So we've developed some very deep relationships."

An early team member to join the firm was Becca Followill, who signed on to lead research and cover midstream companies and MLPs. King says Followill's reputation with midstream investors and managers, coupled with the deep MLP investor experience she and former UBS partner Barry Guinn brought to the table, has been important to the firm's success.

### Fueling the economy

As few as three years ago, MLPs were still considered something of a novelty.

"Things have changed dramatically," King says. "You've seen that now the space is larger on a market cap basis than utilities. We calculated the other day that the MLP market cap—if you include the GPs [general partners]—is now larger than the sum total market cap of independent E&P companies in the United States. It's been a massive change."

King explains that historically, large mutual fund complexes haven't been active in MLP investment.

"They'll dabble, but they're starting to get more involved," he says. "The key is they're beginning to look at MLPs as its own asset class. It certainly makes sense to think of it as its own asset class, and they certainly have a unique set of risk return characteristics."

Still, even with the tremendous cash flow that has entered the market, the asset class itself remains "inefficient," King says.

"Despite the significant amount of capital—and we track the institutional capital that has come into the space very closely—that has been outpaced by the amount of additional equity that has come into the market. The fact is, we continue to see significant opportunities for our clients to generate alpha investing in MLPs."

MLPs have become a unique and attractive financing vehicle that has allowed the U.S. to move fairly quickly to

## U.S. Capital Advisors Profile

- Formed in 2010
- Targets a rate of return of two to four times on its capital
- Combines wealth management with capital investment
- Closed on more than $100 million in merchant banking deals
- Research team covers 61 public energy companies, including 25 midstream and MLPs
- Expects most capital markets business growth from the investment banking business
- Expanding Dallas office in 2014

restructure the infrastructure needs generated by the different sources of natural gas and crude that's now driven by unconventional production, he says.

"MLPs have been a key ingredient in fueling the healthy growth of U.S. energy infrastructure investment," King says, adding, "It's great for the country."

**Expanding the platform**

Last year, the firm stepped up its investment banking activities, taking on the role of co-manager in four energy transactions: the initial public offering of Plains GP Holdings LLC, Oiltanking Partners' first follow-on transaction and deals with Goodrich Petroleum Corp. and Gulfport Energy Corp.

"When I look at the capital markets business, our investment banking business is where I think we have the most significant opportunity to grow," King says. "Despite being a young firm, we are able to compete effectively against both the larger, regional and energy boutique firms as a co-manager because of our unique business model. Our combination of energy focus, longstanding institutional relationships and retail distribution capabilities is a real differentiator for our clients."

In the merchant banking business, the firm advises and raises capital for private companies. That also presents attractive growth opportunity, King says.

The firm will often take a portion of merchant banking fees earned in the form of equity of the underlying issues. That ties U.S. Capital's economics more closely to those of the investors who supply the capital, he explains.

An experienced management team is chief among the attributes the firm looks for in a new deal.

"We like existing, high cash-flow businesses," King says. "Not that we wouldn't do it, but we're less interested in venture-type, early-stage transactions. We like businesses that have a fairly significant amount of visible cash flow that we can see and model."

Many energy-dedicated funds have become so large that, unless a deal is worth deploying several hundred millions in capital, it won't move the needle, King says.

"We see a huge opportunity in the $15 million to $100 million range. That has become a fairly inefficient market because a lot of the players have just gotten too large," he adds.

However, a transaction for one of those smaller companies, such as Badger Midstream Energy LP, is meaningful for U.S. Capital.

The Badger deal was brought to U.S. Capital by Michael McConnell, a director in the firm's merchant banking group. Participating alongside the sponsor and another investor, U.S. Capital took the financing opportunity and raised about $24 million in April 2013. The deal gave Badger the money it needed to complete the acquisition of Midstream Energy Service, a private company based in Tulsa, Oklahoma.

But not all companies want the added governance that may accompany seed money from a large private equity firm, he notes.

"Many do—it's a highly successful model—but it just depends on who it is and how much control and autonomy they want to have to build the business," he says. "We often will take board seats, but we rarely would take a control position." ■

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*The 25 million cubic feet per day capacity Grey Badger plant near Panhandle, Texas, is designed for condensate stabilization, among other uses.* *Source: Badger Midstream Energy LP*


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