

PASSI

Some guys buy an old boat, fix it up and sell it; maybe make a few bucks, maybe not. Stephen Julius and Stephen Heese buy old brands, give them a new life, and sell them at a tidy profit.

Julius and Heese, aka The Two Steves, specialize in reviving heritage brands, i.e., companies that once claimed a special place in hearts and minds but that have since fallen on hard times, gone bankrupt or disappeared.



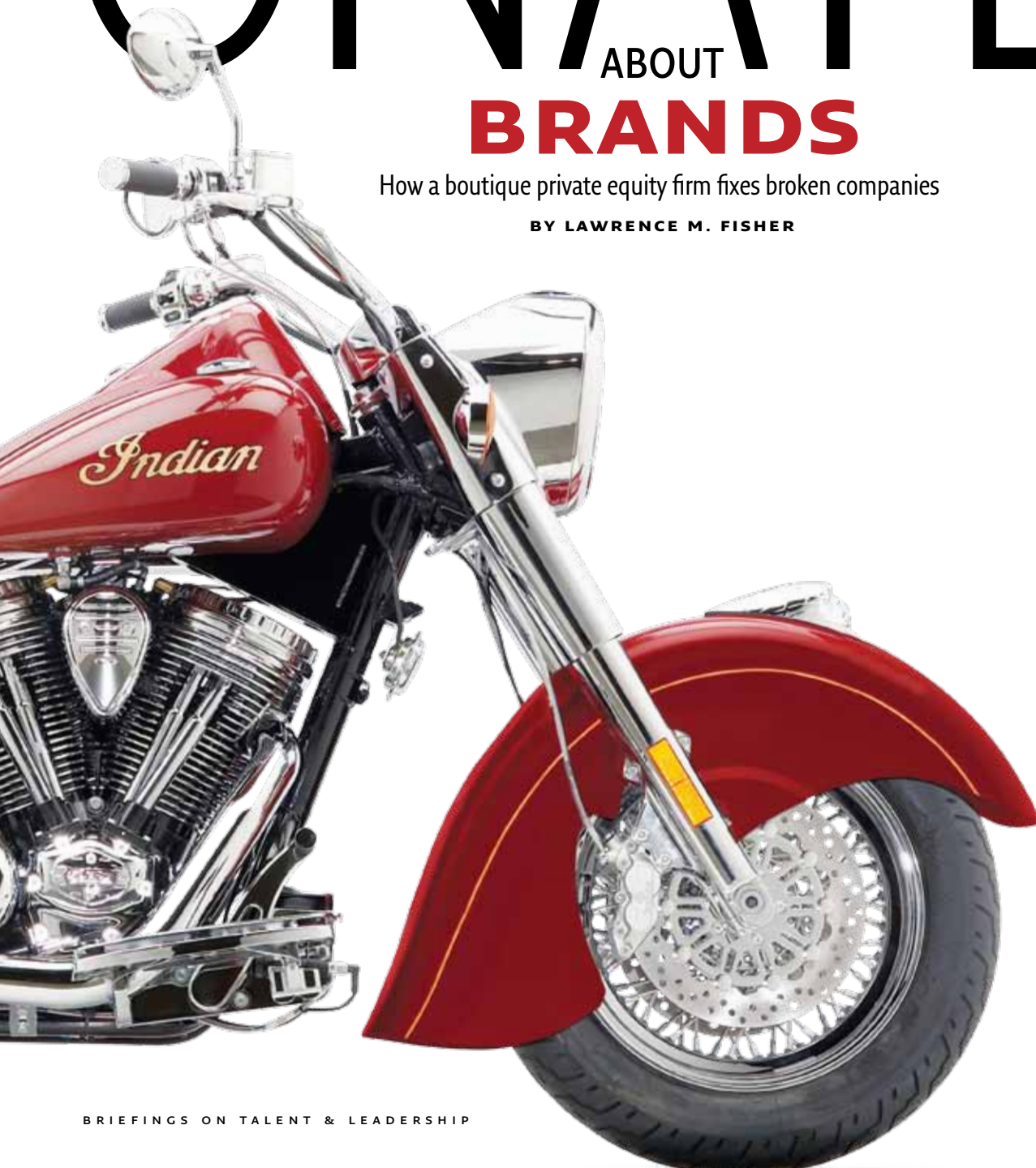
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ABOUT

BRANDS

How a boutique private equity firm fixes broken companies

BY LAWRENCE M. FISHER



A heritage brand can exist in almost any category, from

Through Stellican Ltd., their London-based private equity firm, they have bought, rebuilt and sold Cantiera Riva, an Italian maker of luxury power boats founded in the mid-1800s, and Indian Motorcycle, the oldest motorcycle brand in America. These days the Steves are focused on Chris-Craft, the iconic American yacht manufacturer they purchased out of bankruptcy in 2001.

“I look for certain types of brands, of which heritage is one attribute,” said Julius, who works from Stellican’s

The reborn Chris-Craft power yachts do just that, said Heese, who works at the boat company’s headquarters in Sarasota, Fla. “When people hear ‘Chris-Craft,’ it evokes feelings of a time when America was pure, of elegance and classic beauty. It’s the ‘On Golden Pond’ feeling. It’s that imagery: It’s the Kennedy’s, Hyannis, Nantucket.”

The Steves met at Harvard Business School in the ‘80s. Julius had come to Harvard to study government at the Kennedy School, after taking a First in Classics from Oxford. Heese had a B.S. in management from Tulane Uni-

versity, with a concentration in accounting and computer science. He was also a CPA, licensed in Florida. Among things they had in common, they say, is that both had grown up in strict Catholic families and attended British boarding schools.

After Harvard, Julius worked in the London office of The Boston Consulting Group, specializing in competitive strategy analysis and implementation for multinational clients, with a particular focus on Spain and Italy. Heese spent four years with PricewaterhouseCoopers, before becoming managing director of ERICO International Corporation, a construction products company with operations in 16 countries. He lived in Asia, Australia, the Netherlands and the U.K.

But Julius and Heese stayed in touch over the years and reunited to found Stellican in 1991. The firm was based on the simple proposition that distressed situations presented an overlooked opportunity to create value through the infusion

of new capital and the application of sound management processes. Their strategy was intentionally opportunistic, hence focused on no particular market sector. Indeed, the firm’s early successes were in unglamorous fields such as cash registers and currency exchanges.

“Stephen’s thesis was that there was opportunity in distressed situations, and he was right,” said Heese. “Stephen figured out that when there are not a lot of buyers at the auction, you can buy a dollar for 25 cents. But you need to write a check at the end, and it happens quickly.”

The pair’s ability to move quickly was instrumental in their acquisition of Riva, the Italian company whose boats were practically synonymous with “la dolce vita.” The Riva family had lost control of the company in 1969, and it passed



Fun on 1941 Chris-Craft Runabouts

London office. He seeks out “authentic brands, aspirational brands that have high craftsmanship and premium price positioning. Whether it’s Chris-Craft, Riva or Indian Motorcycle, they all checked all of those boxes.”

Julius and Heese like boats and motorcycles, but they say a heritage brand can exist in almost any category, from shirts to shotguns. The trick is distinguishing heritage from has-been.

“There are brands that may be heritage but need to die and stay dead,” said Julius. “The brands I bought are brands that can be relaunched and be made relevant again. That means making them beautiful. These are all luxury products, so they need to trigger an emotional response from the consumer.”

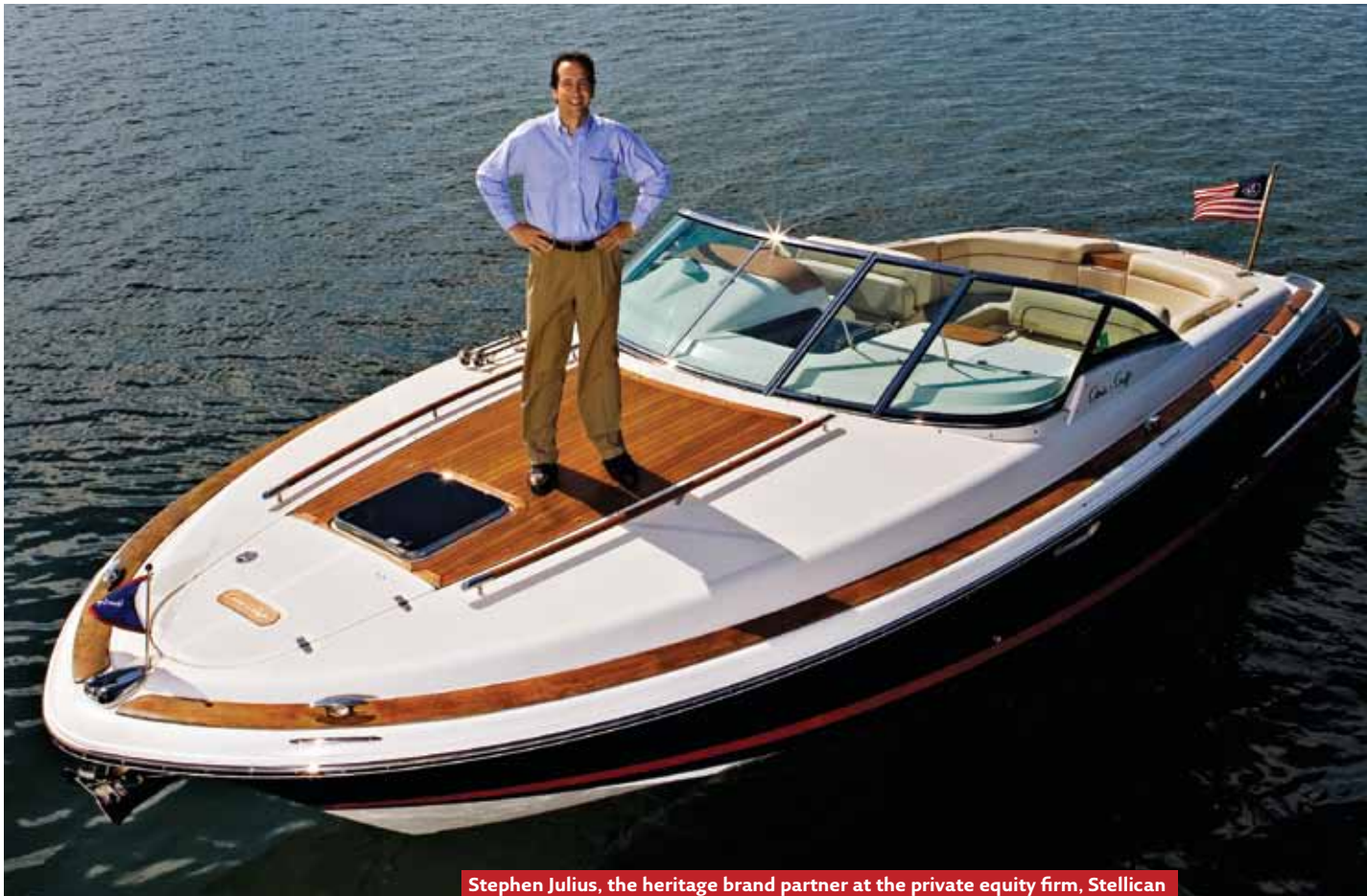
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through a number of hands, ultimately to Vickers Rolls-Royce. “Riva was the Ferrari of boating,” said Heese. “It was owned by Rolls-Royce, which did nothing but lose money. Stephen had been after them for years. They called him on a Monday and said, ‘If you can close by Friday ...’”

Stellican acquired Riva in 1998 and re-established the brand with a fleet of new models, including the much-lauded Aquariva, which took its look and feel from boats

these brands. Why was what was so obvious to us not obvious to them?”

Among the reasons may be that, when investing primarily for their own accounts, Julius and Heese can take a longer view than a corporation or a fund answerable to shareholders for quarterly returns. They also have a bigger appetite for risk, backed up by the kind of confidence in their own abilities that comes with repeated success. But



Stephen Julius, the heritage brand partner at the private equity firm, Stellican

like Riva’s Aquarama of the 1960s. With Riva, Julius first showed his natural flair for fashion, producing a line of boats that evoked a classic era yet steered clear of slavish replicas. The new Riva caught the eye of Ferretti Yachts, Italy’s largest maker of pleasure craft, which acquired the company from Stellican in 2000.

“We take something that’s completely broken, re-launch it and sell it to a large corporation that could be the natural guardian of that brand,” said Julius. “It is interesting that major corporations, given the opportunity, don’t buy

what really sets Stellican apart may be the complementary combination of skills embodied in its two principals.

Julius is Mr. Strategy, but he is also Mr. Style, shepherding the look and feel of Stellican’s brands and their products at a granular level of detail. He speaks in rapid-fire sentences, his Anglo-Italian parentage apparent in the mixture of clear-headed calculation and unabashed enthusiasm he exudes. Heese is Mr. Operations, a veteran of hiring and firing and building teams, but he is also Mr. Sales, managing both dealer and customer relations with a natural

Courtesy of Chris-Craft

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ease. He grew up in Tampa, Fla., and is happy to be home.

“Our relationship works; it’s probably best left unexamined,” said Heese. “Stephen’s really good at styling, design, colors, materials and the things the customer sees. He leaves everything else to me and the team here. He’s passionate about product, passionate about marketing. He hasn’t been in the warehouse in 10 years. He’s a purist.



Steve Heese, the operations partner in the private equity firm, Stellican

Like me, he wants to see it done right, and if it doesn’t sell, we’re better off than if we’d cheapened it to make it sell.”

The acquisition of Indian Motorcycle in 2006 tested Stellican’s resources and resolve. Founded in Springfield, Mass., in 1901 as the Hendee Manufacturing Company, Indian became the largest manufacturer of motorcycles in the world, but ceased operations in 1953 after a long period of decline. For periods during the 1950s and ’60s, various British and Italian motorcycles were imported to the United States and labeled as Indians, some of them evidently without the importers having obtained licensing rights to the trademark.

The brand was long gone by 1998, when the Federal District Court of Colorado awarded the Indian trademark to a consortium that included the manufacturer California Motorcycle Company (CMC) and IMCOA Licensing America Inc. The new company began manufacturing motorcycles in 1999 at the former CMC’s facilities in Gilroy, Calif.

But despite a capital infusion of \$200 million, the bikes were plagued by technical problems and manufacturing defects, and the new Indian entered bankruptcy in 2003.

Most potential buyers viewed the remains and passed, but Julius saw a unique opportunity to establish a premium alternative to Harley-Davidson in the market for so-called heavy twins, large motorcycles with vertical two-cylinder motors. Within that niche, Harley has a 78 percent market share, even though all four of the big Japanese motorcycle manufacturers produce such bikes.

“Only Harley was considered an authentic brand, and authenticity is essential to that segment,” said Julius. “The only brand on the planet that could compete with Harley was Indian Motorcycle. That was a complete no-brainer. It didn’t take too much reading of business professor and strategist Michael Porter to realize there was an opportunity there.”

The challenge was that Indian would require far more than the \$10 million in equity capital that was typically Stellican’s ceiling. “Indian was the first deal that wasn’t [done with] all our own money,” said Heese. “There were lots of plans we could pursue, and had we done it with all our own money, it would have sold the brand short. We made up a list of all the people who had said, ‘if you ever need money,’ and the first guy we went to put up the whole deal. He didn’t want to be named — and he was a great partner.”

Stellican acquired Indian for a reported \$30-something million in 2006 and re-established the company in Kings Mountain, N.C. The first bikes debuted in December 2008 to positive reviews from the motorcycle press. Notably, the revived-again Indians commanded a premium price from the outset, about 50 percent more than comparable models from Harley.

“Our strategy is consistent: Come in at the top,” said Heese. That means “no compromises, lots and lots of chrome, real leather seats, no plastics. The Japanese bikes are loaded with plastic, and all Harleys come with vinyl seats. We gave Indian a show-car quality paint job. But, like for like, theirs is \$19,900, ours is \$29,900. It means there are fewer buyers there, but there are buyers there.”

And in short order, there was a buyer for the whole company. Polaris Industries Inc., a leading maker of snowmobiles and parent company of Victory Motorcycles, agreed to purchase Indian from Stellican in April 2011.

Courtesy of Chris-Craft

“It speaks volumes to what Steve and Steve could do, to step in and start pulling together this fragmented business and bring it back to life,” said Scott Wine, Polaris’ chief executive officer. “They got the revival started and really let us pick it up along the way. We would probably not have had the heart to take it all the way right out of bankruptcy, and they did that hard work. But we are the perfect business to take it to the height Stephen [Julius] had envisioned, and he doesn’t become so attached that he doesn’t know when to let go.”

The purchase price was not disclosed, but the Steves say the deal met their expectations. “We’re disappointed if

That strategy recognized the fact that all steep curves are prone to flatten.”

Chris-Craft is a different story. Unlike Indian, which at least came with some viable designs and tooling, Chris-Craft had been so cheapened by the succession of previous owners that Stellican essentially started from scratch.

The Steves hired Michael Peters, a naval architect whose design portfolio includes everything from 200 mph-plus offshore world champion catamarans to 100-foot-plus megayachts, and challenged him to create a suite of new Chris-Craft models that combined classic style with modern performance. Heese opened a new



Chris-Craft’s Corsair

we don’t make internal rates of return north of 35 percent, simply because of the risk we’re taking,” said Heese. “When you buy trademarks at auction and invest everything required, you deserve a good return and — knock on wood — we’ve never had a loss. And we’ve achieved our objectives; even in a down economy we’ve done well.”

Because there are only two Steves, Stellican is limited in the number of deals it can pursue, and it has passed on brands the principals would have dearly loved to acquire.

“It’s just Stephen and I, so we don’t have the bandwidth to do more than two at a time,” said Heese. Normally, he added, they also try to turn brands quickly. “At the beginning, the value creation curve is very steep. Before Chris-Craft, the average investment time was less than 24 months.

factory in Florida, where he was able to tap into a rich existing vein of boat-building skills.

The new Chris-Craft models have hull shapes recognizable from a mile away, yet also feature rich detail work such as abundant real teak and clever retro touches such as a perforated metal dashboard. As with Riva and Indian, Stellican’s Chris-Craft came in at the top, with yachts priced about 50 percent higher than their plainer rivals. Ranging from 20 to 36 feet, they are priced from \$47,000 to \$550,000.

For powerboat lovers, the new Chris-Craft boats push all the right buttons. Reviewing the flagship Corsair 36 in *Yachting* magazine, Jay Coyle wrote: “Given 36 feet to play with, Chris-Craft’s latest addition to its Corsair line is not

the sort of product that most production boat bean counters would come up with. ... Let's just say she is a beautiful boat with excellent performance and a pedigree that extends further back into yachting history than most of us can remember."

Indeed, few American brands can claim as rich a history. Born in 1861, the first year of the American Civil War, Christopher Columbus Smith built his first "duck boat" in 1874. He went on to develop the first boatbuilding company to produce standardized designs, adopting the Chris-Craft name in 1924. Vanderbilts, Sloanes, Morgans and Fords were Chris-Craft owners, as were F.D.R., J.F.K., Frank Sinatra, Katherine Hepburn and Elvis Presley. And yes, that is a vintage Chris-Craft piloted by Henry Fonda in "On Golden Pond."

Chris-Craft buyers like the history, but the brand also delivers a high level of style and substance, said Jerry Ipjian, an owner of dealerships around the Great Lakes and in Florida. "When a guy buys a Ferrari, it's for the looks, the feel. People buy those things for the quality and distinction, so they don't look like everybody else. That's exactly what Chris-Craft does. It's an attention getter, it's quality, it's elegant. I've pretty much eliminated other boats."

Had everything gone according to plan, Stellican probably would have sold Chris-Craft by now. But with two young children, Heese was tired of chasing deals and moving every two years, and Julius was amenable to holding on, even as the offers began pouring in.

"We made a lifestyle choice not to sell Chris-Craft when the phone was ringing off the hook in '06 and '07," said Heese. "After selling Indian, we made a decision that Chris-Craft is going to be our platform. We don't know exactly what that means. We started with zero; in '08 we did \$60 million, and we saw a clear path to \$100 million. Little did we know the world would go into a death spiral. So last year we did \$30 million and in calendar [year] '11, we'll do \$40 million."

Of course, if the world slips back into recession, all bets are off. No one needs a power boat, or any kind of recreational watercraft, and the entire industry has been in the doldrums for years. Bill Basler, president of the Chris-Craft Antique Boat Club, notes that the Smith family was notoriously frugal, and aimed to build boats for "everyman," as Ford had automobiles. Chris-Craft weathered the Great Depression by introducing stripped-out models, called Utilities, that sold for as little as \$595, when most powerboats were \$1,500 to \$2,500.

When Julius and Heese acquired Chris-Craft, "I believe it was their desire to make it a prestige brand," Basler said. "That becomes the marketing challenge to me. Prestige means you're not going to be everyman's Chris-Craft anymore. It's going to be a high-priced boat. The question for

the long haul is: Is that the right approach? Or can you be a prestige brand and have economical offerings as well?"

Many boat companies have cut costs in recent years by moving manufacturing to Asia, but Heese said it is important for Chris-Craft to be made in the United States. "If you think about the feelings that the brand evokes, it evokes feelings of a time when America was more innocent than it is now, and people want to know where they're built," he said. "If you stand at a boat show, over the course of a week you will get asked that question a lot."

One way to use Chris-Craft as a platform is to extend the brand into bags and apparel, a strategy that has worked well for sporting goods companies ranging from Patagonia, originally a maker of specialized mountain-climbing equipment, to Burton Snowboards. Harley Davidson has a popular line of leather jackets and other bike-related clothing, which Stellican successfully emulated at Indian.

But such platform plays are more difficult than they look, said Michael Jager, a brand design specialist who has worked with Patagonia and Burton, as well as Levi's and Nike. Customers today crave authenticity, particularly from heritage brands, so any line extension that seems opportunistic or fake in any way risks alienating the very people you want to attract, he said.

"To own a heritage brand with the word 'craft' in the title now is just brilliant, that's everybody's dream," Jager said, noting that Levi's newest brand is called "Made and Crafted." "But the transition from something so powerful as a powerboat to apparel is a tricky one. I can imagine a Chris-Craft apparel line that really had insight, that really was about being on the water, but it would have to have excellent workmanship and utility."

Julius and Heese say they will ensure that any extensions of the Chris-Craft brand meet their standards for high quality. They intend to keep all product development in-house, but will seek out manufacturing partners with proven track records. And Julius said that apparel is just one option. He has not ruled out sailboats, which the original Chris-Craft built alongside its better-known power yachts, and he believes the brand name can be extended to a wide range of water- and sea-related items.

Nor is Stellican done buying heritage brands, Julius said. The company made a play for MG, the classic British sports car brand, going so far as to strike a deal with Bob Lutz, then vice chairman of General Motors, to produce cars on the Pontiac Solstice chassis, but were outbid by the Chinese. He says he is constantly on the lookout for brands that are authentic, aspirational and acquirable.

"I'm passionate about brands," Julius said. "I can envision products; I can conjure up lifestyles around that brand. Maybe other people would call it creativity. I would call it common sense." 