

Fulcrum: *underwriting a co-investment* in a \$520M specialty-distribution buyout.

A sponsor on the LP's approved-funds list offers a \$40M fee-free, carry-free co-investment alongside its \$260M equity check in the buyout of a North American specialty-distribution and business-services platform. Entry is 10.0x EBITDA at 5.0x leverage. Fulcrum is the independent underwrite: an operating case, a leverage and returns model, and a sensitivity that locates where the deal breaks, delivered as a go/no-go the IC can vote on.

Author S. Ize-Iyamu **Audience** Investment Committee **Length** 3 pages **Status** Co-investment underwriting
Sleeve Funds & Co-Investments

The Opportunity

The economics are the reason to look; the underwrite is the reason to commit. A no-fee, no-carry co-investment lets the LP keep the gross deal return instead of paying the 1.75% fee and 20% carry it would bear on the same dollar inside the fund, an edge worth on the order of 7-8% of IRR (Cambridge Associates). That fee saving, not superior deal access, is the structural case for a co-invest program; it holds net only for an LP that diversifies across deals and underwrites each one independently, on the sponsor's timetable, since one-off co-investments can suffer adverse selection. **The deal:** a \$520M-EV buyout of a specialty distributor at 10.0x \$52M EBITDA, financed with 5.0x leverage (\$260M) and \$260M of equity, of which the LP takes \$40M (15%). **The thesis:** a fragmented end-market, a tuck-in runway, and a pricing-and-procurement program that lifts EBITDA from \$52M to roughly \$78M over five years, with returns earned on operations and deleveraging, not multiple expansion, against a rate-exposed float.

FIGURE 1 · SOURCES & USES · ENTRY SNAPSHOT

SOURCES & USES · \$520M ENTERPRISE VALUE

SOURCES		USES	
Senior + sub debt (5.0x)	\$260M	Equity purchase price	\$505M
Sponsor equity	\$220M	Transaction fees & financing	\$15M
LP co-invest equity	\$40M		
Total sources	\$520M	Total uses	\$520M

CAPITAL STRUCTURE



\$520M EV at 10.0x entry, half funded by debt. The LP's \$40M is 15% of the \$260M equity and 8% of total capitalization. Fee-free and carry-free, so gross equals net for the co-investor.

The operating case

The thesis is not heroic: **6% revenue CAGR** and **150 bps of margin expansion** from a procurement program, disciplined pricing, and three to five tuck-in acquisitions, carrying EBITDA from **\$52M to \$78M** (an 8.5% CAGR). The base case applies a **conservative half-turn of multiple contraction** at exit (9.5x vs 10.0x entry), so the return is earned on operations and deleveraging rather than a re-rating. A free-cash-flow sweep pays roughly **\$110M** of debt over the hold, dropping net leverage from 5.0x to under 2.0x and converting enterprise growth into equity.

Entry at 10.0x sits mid-band for 2024 mid-market buyouts; the 9.5x exit is held conservative relative to recent levels (see Sources).

LP CO-INVEST CHECK

\$40M

fee-free · carry-free

BASE-CASE RETURN

2.3x

18% IRR · 5-yr hold

EBITDA GROWTH

\$52 → \$78M

8.5% CAGR

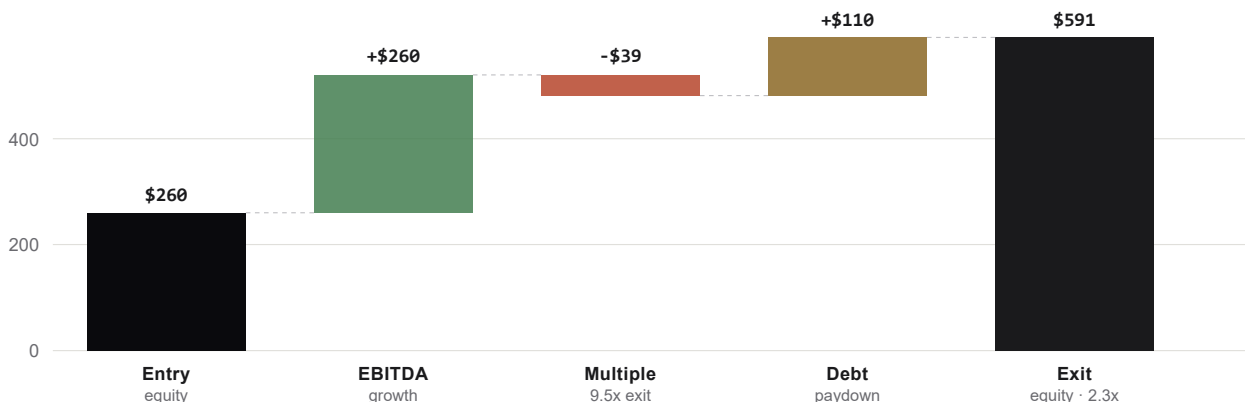
THE UNDERWRITE

Build the return from three independent levers and test each: **EBITDA growth** (does the operating case hold without the bolt-ons, which carry integration risk?), **multiple change** (underwrite to contraction, treat any expansion as upside), and **debt paydown** (how much of the return is just the sponsor's leverage, and how rate-sensitive is the float?). A clean co-investment is one where operational value, not financial engineering, is the largest bar in the bridge, and where the deal still clears the LP's hurdle under a one-turn-down exit and a higher-for-longer rate path.

Where the return comes from

FIGURE 2 · EQUITY VALUE BRIDGE · ENTRY \$260M → EXIT \$591M (BASE CASE)

EQUITY VALUE BRIDGE · \$M · BASE CASE · 5-YEAR HOLD



Operational EBITDA growth (+\$260M) is the largest contributor and clears the bar for a clean co-invest; debt paydown (+\$110M) adds the sponsor's leverage; a conservative half-turn of multiple contraction (-\$39M) is underwritten, not assumed away. \$260M entry equity becomes \$591M, a 2.3x gross-equals-net for the fee-free co-investor.

The shape of the bridge is the underwriting test: in a clean co-investment the EBITDA-growth bar should dominate, with debt paydown a supporting contributor and multiple change a small, deliberate drag rather than the engine of the return. Here operational value far outweighs the multiple effect, so the deal does not rely on selling into a richer market than the one it was bought in.

WORKED EXAMPLE · BASE-CASE RETURNS MATH

Exit EV = $9.5x \times \$78M = \$741M$; exit net debt **\$150M** (from \$260M, after a \$110M FCF sweep); exit equity **\$591M**. On \$260M of entry equity that is a **2.3x MOIC / 18% IRR** over five years. The LP's \$40M tracks the syndicate pro-rata at **\$91M**, and because the co-invest is fee-free and carry-free, the 2.3x is also the net number, versus roughly **1.9x net** for the same dollar inside the fund after a 1.75/20 load, a 1.2x uplift that is the whole point of the program.

Sensitivity · IRR to exit multiple and EBITDA CAGR

BASE-CASE IRR ≈ 18%	EBITDA CAGR 4%	CAGR 6.5%	CAGR 8.5% (BASE)	CAGR 11%
Exit 8.5x (-1.5 turns)	6%	9%	12%	15%
Exit 9.5x (base)	11%	15%	18%	22%
Exit 10.5x (flat re-rate)	15%	19%	23%	26%

Read down the base-case column: the underwrite holds a double-digit IRR even if the exit multiple compresses a turn and a half to 8.5x, and it slips below the LP's 12% hurdle only when that contraction coincides with a near-stalled operating case (4% EBITDA CAGR). That joint scenario, not either factor alone, is what the rate hedge and the operational diligence are built to protect against. The grid also frames the sizing decision: because even the bear corner returns capital, a \$40M check lets the sleeve absorb the downside without impairing the vintage.

IRRs modeled on the base-case operating plan and a five-year hold.

Underwriting scorecard

DIMENSION	METRIC	UNDERWRITE	WHY IT MATTERS
Return quality	Operational share of value bridge	79% (EBITDA growth)	A clean co-invest is earned on operations, not leverage
Entry discipline	Entry multiple vs comp range	10.0x (mid of band)	No reliance on a re-rating to make the return
Leverage	Net debt / EBITDA at entry → exit	5.0x → < 2.0x	Deleveraging converts growth into equity
Rate exposure	Floating-rate debt share	60% (hedge required)	An unhedged float can erase the FCF sweep
Downside	IRR at 8.5x exit / 4% CAGR	6% (above zero)	No capital impairment in the modeled bear corner
Alignment	Sponsor equity beside the LP	\$220M (5.5x the LP)	Sponsor takes first-dollar risk on the same terms

Risks & mitigations

- HIGH** **Cyclicality of end-market demand: specialty distribution volumes track industrial and construction activity, and a downturn compresses both EBITDA and the exit multiple at the same time.**
Mitigation: underwrite the base case to a half-turn contraction and stress the joint bear corner (bottom-left of the grid); confirm end-market diversification and the share of recurring/consumable revenue; size the LP check so a 1.0x outcome is survivable within the sleeve.
- HIGH** **Interest-rate exposure on floating debt: with 60% of the structure floating, a higher-for-longer path raises cash interest and slows the FCF sweep that drives a third of the return.**
Mitigation: condition the commitment on an interest-rate hedge (cap or swap) covering at least 75% of floating debt for the first three years; model the un-hedged case explicitly as a downside in the IC memo.
- MED** **Co-investor information asymmetry and timeline: the LP underwrites on the sponsor's data and clock, with fewer information rights than the sponsor and a hard signing date.**
Mitigation: negotiate information rights, quarterly reporting, and tag-along/exit-alignment provisions; rely on the sponsor's confirmatory DD but rebuild the model independently.

30 / 60 / 90: from offer to close

WEEKS 1-2	WEEKS 3-4	POST-CLOSE
Independent model <ul style="list-style-type: none"> › Rebuild the LBO from the data room, not the deck › Operating case stress-tested without bolt-ons › Hedge and covenant terms confirmed with the sponsor 	IC & terms <ul style="list-style-type: none"> › Go/no-go memo with the sensitivity grid › Information rights and tag-along negotiated › Allocation confirmed; legal documentation 	Monitor <ul style="list-style-type: none"> › EBITDA-bridge actuals vs underwrite, quarterly › Net-leverage and hedge mark tracked › Exit-readiness reviewed against the multiple thesis

DECISION ASKED

Approve a **\$40M co-investment** alongside the sponsor on a **fee-free, carry-free** basis, conditional on an **interest-rate hedge covering ≥ 75% of floating debt, information rights with quarterly reporting, and tag-along / exit-alignment provisions**. **Pass** if the hedge or information rights are unavailable, or if confirmatory diligence cannot support operational value as the largest bar in the bridge. **Success:** the IC votes on an independent underwrite that clears the hurdle under a one-turn-down exit and a higher-for-longer rate path.

Sources: entry multiples and leverage per PitchBook LCD (2024); co-investment economics per Cambridge Associates and Braun, Jenkinson & Schemmerl (JFE, 2020), with the adverse-selection view in Fang, Ivashina & Lerner (JFE, 2015); exit-multiple context per PitchBook mid-market data (2024).