

## **Booz Allen-Carlyle Group: The Buy-in Deal Goes On**

*This article was written by Michael Lent, publisher of **Government Services Insider**, an independent source of insight and commentary on the professional and IT services firms that serve the federal government. Now in its fifth year of publication in January, the Insider focuses on successful business strategies, lessons learned, best practices and critical inputs to thinking through improvements in business management and development. Contact: [www.gsinsider.com](http://www.gsinsider.com) or [editor@gsinsider.com](mailto:editor@gsinsider.com) or 202.237.0765 for subscriptions or other information.*

While both privately held firms remain mum, there is ample evidence that the deal-making goes on between venerable consultant/contractor Booz Allen Hamilton and the Carlyle Group, one of the top private equity firms.

The emerging deal is attracting lots of attention in the industry because of the recent dip in large M&A transactions, the small presence of PE firms in the government services arena, as well as the mystique about Booz Allen's government business, which is in the \$3.5-4.0 billion revenue range.

Publicly, the Booz Allen press spokeswomen, while not referring to Carlyle or a deal, has referred in a public statement to "tension" between the government and commercial businesses of Booz Allen. Also, and with circumspection, Ralph Shrader, Booz Allen CEO, told the firm's alumni last month that the firm is:

*"... considering a significant change in strategic direction that could lead to our commercial and US government businesses operating as separate firms in the future. In discussions with Booz Allen partners around the world, we have found strong support for the view that the long-term success of our two major businesses could be enhanced by complete focus on their distinct markets....*

*If we determine that a strategic opportunity is in the best interest of the firm, partners, employees, and clients, it would be brought back to the Board of Directors and then to all of the active officer-shareholders for a vote."*

It would be mistaken to view this as a buyout. Rather, from sources who would know solid particulars, it is a "buy-in," or really a large-scale borrowing that will enable the complete separation of the two Booz Allen businesses.

Though a closely held Delaware corporation, Booz Allen has about 320 shareholding vice presidents who run the firm much like a partnership. Two-thirds of them are in the firm's traditional commercial consulting business, which has grown little during much of the last decade, while the government business has expanded 10 to 20 percent annually. The government business accounts for about 85 percent of the firm's 20 thousand

employees and a similar proportion of its total revenue and profit, according to our sources.

However, there are about two commercial partners for every government partner in Booz Allen. And the government partners have been bringing home the bacon for all partners in the firm for a long time. According to our sources, that's a primary source of the "tension," as well as a significant cultural gap between the two businesses. Furthermore, the government business is in a better position to chart and deliver further growth.

So, the purpose of Carlyle's involvement will be to finance the buyout of the Booz Allen commercial partners' interest in the Booz Allen government business. Carlyle may be issued stock (possibly a minority share) and warrants, some sources say, but its biggest stake will be in medium-term debt financing on the order of one to two billion, according to very rough estimates. And almost all the assets involved are intangible. The security is really a set of people, their current contracts for services, and their prospects.

Our sources also suggest that the loan repayment to Carlyle will be from incremental growth, which has slowed for all firms in the federal services business recently. Regardless of projected buoyant IT and military hardware spending in the president's proposed budget, even a well positioned business, such as Booz Allen's, will find growth more difficult as the business overall gets tougher over time.

Speaking of time, this won't be a short-term deal. Clearly, it isn't a precursor to a flip that some PE firms engage in because Carlyle's role in this is as financier, rather than a full or majority owner directing the business. Second, the indications we see is that most Booz Allen government business partners want to stay in their robust business. If the deal completes, it is expected to close by March 31, the end of the firm's fiscal year.

But some have voiced concerns about the tight rationing of information about the deal. As in any restructuring, there may also be some departures of partners and valued staff who would rather not deal with the inevitable uncertainties ahead.

Other concerns we have heard from people in the government business include: the anticipated accelerated pace of business in order to meet Carlyle debt repayment requirements on top of the firm's own stretch goals for revenue and profit; the possibility of cost-cutting that may alter the distinctive, successful culture; and how to explain to clients the revised brand of a stand-alone Booz Allen government business.

All of this said, however, it is hard to imagine a stronger pairing than the skilled and experienced (including with government contractors) Carlyle as investor and Booz Allen as a robust borrower and leader in the government business.