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Washington Climbing as a Financial Center

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Until this week, you'd probably never heard of John Delaney. But he's one reason Washington has quietly elbowed its way into the second tier of financial centers in the United States, alongside San Francisco, Chicago, Boston and L.A.

A lapsed Georgetown-trained lawyer, Delaney raised \$500 million in equity back in 1999 and began making customized loans to mid-size companies, a market largely abandoned by commercial banks. With a net interest rate spread of nearly 10 percentage points, CapitalSource turned out to be a good enough business to take public this week, raising another cool \$232 million. At the close of trading yesterday, the Chevy Chase firm was valued at \$2.1 billion, giving 39-year-old Delaney a stake worth \$160 million.

Also on a roadshow this week was David Gladstone, who at Allied Capital virtually created the business of mid-market "mezzanine" lending. After a bitter split with Allied, Gladstone helped Malon Wilkus build a rival operation at American Capital Strategies in Bethesda, which boasts a \$2 billion loan portfolio. Now on his own at Gladstone Capital, he's raising \$80 million to finance buyouts of firms by lending against their real estate assets.

All this is taking place in a tough market for public stock offerings. So it is noteworthy that Arlington-based Friedman, Billings, Ramsey has held its own against much bigger and more prestigious Wall Street investment banks in this year's IPO sweepstakes.

These are just some of the firms that now constitute a critical mass of financing activity necessary to attract big money and talent to Washington and create synergies among the firms.

In the buyout world, Washington's Carlyle Group may be the world's biggest pool of private equity, while Frank Pearl's very private Perseus Group now has \$2 billion under management. Although Fred Malek's Thayer Capital has taken some hits, he recently raised another \$300 million in equity and signed on a former chief financial officer from IBM. Former Bell Atlantic chief Ray Smith heads up Arlington Capital Partners, with \$450 million to invest. And First Brother Marvin Bush, along with Scott Andrews, a former WorldCom chief financial officer (he left in '94), manages \$780 million at Winston Partners in McLean.

Several firms have sprung up offering investment banking and strategic advice along with their financing. The list includes G. William Miller & Co., headed by the former Treasury secretary; Promontory Capital, whose principals include former comptroller of the currency Gene Ludwig and former Fed governor Alan Blinder; and Milestone Merchant

Partners, which is working with former SEC chairman Richard Breeden on MCI's restructuring.

Washington's venture capital community has emerged from the tech bust humbled and diminished but probably in better shape than VCs elsewhere. Survivors include old stalwarts like New Enterprise Associates and Novak Biddle and newcomers like Core Capital, Venturehouse Group and Valhalla Partners.

All of these take their place next to mortgage kings Fannie Mae and Freddie Mac, a renamed and privatized Sallie Mae for student loans, and the World Bank Group, the first port of call for developing countries looking for project financing.

The story here may be that Washington's weaknesses as a financial center have now become its strength.

Because Washington financiers tend to be former lawyers, corporate executives and government officials who didn't climb the traditional Wall Street ladder and don't work in the New York hothouse, they are more apt to think outside the box and avoid the Wall Street groupthink that leads inevitably to lower investment returns.

And while American investors may view government as the enemy of business, foreigners actually prefer money managers with good political connections and antennae.

Most important, Wall Street thrives when the big money is in financial engineering and short-term trading. But the post-bubble environment now favors the kind of private equity investing and long-term lending in which Washington excels.

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