Inside the Mind of an Acquirer

Understanding the Potential Buyers of Your Business

The **Value**Builder System™

Like bungee jumping, getting married, or hiking the Grand Canyon, selling your business is something you're likely only going to do once in your life. There's no practice tee and no batting cage, so it's worth doing a little planning beforehand.

In this eBook, you'll get inside the mind of an acquirer.

By understanding the motivations, the business models, and how each type of acquirer invests, you'll be better equipped to make informed decisions about the future of your business. Whether you're looking to cash out and retire or sell part of your company and roll the dice with a new investor inside your business, having a clear understanding of your potential acquirer gives you a leg up.

This eBook is laid out in three parts. First we'll look at the three most common types of acquirers and how they think. Then we'll look at two less commonly known types of acquirers. Think of them as emerging, or sometimes hidden, masquerading as a traditional acquirer. Knowing how they operate can help you punch above your weight in a negotiation with them. Finally, we'll look at the pros and cons of working with each.

For each acquirer type, we'll also zero in on a real-life example so you can hear, in their own words, what they look for when acquiring companies. Each appeared as a guest on Built to Sell Radio, a weekly podcast for business owners interested in selling a business. Built to Sell Radio boasts more than three million downloads and is the ultimate insider's guide to approaching the most important financial transaction of your life.

Let's dive in.

Table of Contents

PART 1

The Traditional Players

Individual Investors

When it comes to your endgame, what's your highest priority? Do you want to maximize your personal wealth and walk away? Do you want to de-risk but keep some chips on the table? Or is your highest priority protecting your culture, your employees, and the legacy you have built? If your goal is to protect your culture, then selling to an individual investor may be worth considering.

Most individual investors are buying themselves a job. They typically don't bring a lot of cash to the table, so they use debt, often underwritten by government programs—like the Small Business Administration (SBA) in the U.S. Because they are using debt, they look for "bankable" businesses, meaning your business can qualify for a bank loan.

What gets them excited are opportunities to roll up their sleeves and make improvements, streamline operations, or tap into new markets to boost your company's value. Sure, they love making money, but they're also drawn to the thrill of getting hands on in managing a business.

The companies they target are generally smaller, often less than one to two million dollars in revenue. Because of this, individual investors will typically pay a modest multiple of seller's discretionary earnings (SDE). When it comes to the kinds of businesses they're eyeing, think buffet versus fixed menu. They're into everything from small home service businesses to quirky distributors of all kinds of stuff.

Individual investors are usually flexible and creative when it comes to making deals. They might offer to let you hang on to a piece of your equity after the acquisition or arrange other unique financing options designed to keep you involved after the sale. Their aim? To make sure everyone's got skin in the game and is committed to making the business a success.

SECRETS to Negotiating with an Individual Investor

Even if you don't need one, make sure your business can qualify for a bank loan by ensuring your books are professionally kept and you have predictable and growing profits.

Inside the Mind of Individual Investor
Connie Fenyo

Connie Fenyo started out as an employee at Dye & Durham, a company that makes software for lawyers. She rose to Executive Vice President when she learned her boss was looking to sell the 200-employee firm.

Fenyo decided to make a bid.

She scraped together all the money she could find, borrowed (in return for a personal guarantee) everything her bank would lend her and got the former owner to finance some of the acquisition price.

That's when she found herself –deeply in debt–as the proud new owner of Dye & Durham. Fenyo had gambled her entire life savings and committed that if she could ever work her way out from under the mountain of debt, she would sell Dye & Durham. And that's exactly what she did.

In this episode, you'll learn:
- How Fenyo financed her purchase at tremendous personal risk
- Fenyo's strategy for prioritizing debt payments while growing her company
- Why selling a business can be its own full-time job

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Private Equity Groups

These acquirers operate by pooling capital from investors and deploying it to acquire ownership stakes in companies. The primary goal for a private equity group? Boosting the performance and overall value of their acquisitions.

Motivated by the allure of significant profits, private equity groups set their sights on businesses with promising growth potential and ample opportunities for value creation. They bring capital to the table and also a wealth of expertise and resources to drive change within the companies they invest in. Whether it's expanding their portfolio or driving down costs, private equity groups are driven by generating returns for their investors. You can expect a private equity group to have a hold period of five to seven years before selling your business.[1]

Private equity groups are typically investors, not operators, which means they will often try to retain the owner of the companies they invest in by asking the owner to stay on as CEO and "roll equity."[2]

In their hunt for the perfect investment, private equity groups generally look for a highly fragmented industry where there are lots of small, independent companies with the potential to be consolidated. Additionally, they will often gravitate toward mid-sized to large enterprises with a minimum of one million dollars in EBITDA that generally have a professional management structure in place and the potential for a bigger exit.

When considering turn-offs, private equity groups mostly avoid companies that have excessive debt or significant regulatory hurdles. They're often cautious around industries prone to volatility or rapid technological disruptions. On the flipside, businesses with strong market positions, recurring revenue streams, and clear avenues for operational enhancements are like magnets to private equity groups.

SECRETS
to Negotiating with a Private Equity Group

Be prepared to co-invest with them as you'll be asked to roll some of your equity.

1. A hold period is the length of time an acquirer will retain ownership of your business before exiting.
2. Rolling equity is an industry term that means taking some of your proceeds from selling your business to reinvest them in the company buying your business.

Inside the Mind of Private Equity Acquirer

Adam Coffey

Adam Coffey spent 21 years as a CEO and investor in three national service companies backed by nine private equity sponsors. During that time, he completed 58 acquisitions and generated more than one billion dollars of value at exit. Adam shared his private equity playbook with Built to Sell Radio, and the episode stands as a rare glimpse inside the mind of a private equity acquirer.

During the episode, Adam discussed how to:

- Become irresistible to a private equity group.
- Optimize your pricing.
- Perform reverse diligence.

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Strategic Acquirers

One of the key differences between individual investors, private equity groups, and strategic acquirers is that both individual investors and private equity groups are looking to make your business more valuable whereas strategic acquirers are looking to make their business more valuable.

Let's say you're a company with one hundred salespeople who call on bicycle shop owners. You've made a substantial investment in hiring and training a nationwide salesforce who are already on a first name basis with bike shop owners across the country. If you spot a struggling, undercapitalized company with a great product carried by few bike shops, a strategic acquirer may reason that adding a new product to the briefcase of their 100 salespeople is an easy way to boost sales.

Strategic acquirers are not just in it for the short-term gains; they're usually thinking long term, seeking out businesses that can blend with their own operations and create a result that's greater than the sum of its parts. They'll generally pay you more than an individual investor or private equity group because the potential upside of improving their business can be huge. Essentially, they view the acquisition as a way to combine forces in order to drive revenue, streamline costs, and cement their position in the market. Unlike an individual investor or private equity group, a strategic acquirer has assets that become more valuable if they own your business. It's not just about owning your company; a strategic acquirer will typically want to integrate your business into theirs.

So what really fires up these strategic acquirers? They want to make their business more valuable, and if your company will help them do that, they may be interested.

Publicly traded strategic acquirers look for accretive acquisitions. For example, let's say a strategic acquirer trades on the stock market at fifteen times EBITDA and they buy your business for seven times EBITDA. It's accretive for the acquirer because when your company is folded into the larger organisation, your profits garner a valuation of fifteen times EBITDA when expressed on their P&L even though they only paid seven times.

SECRETS

to Negotiating with a Strategic Acquirer

Avoid talking about how your business could grow under their ownership. Instead, show them how your company will make their business more valuable.

Inside the Mind of business owner Michael Lieberman and his Experience Selling to a Strategic Acquirer

Michael Lieberman

During his appearance on Built to Sell Radio, business owner Michael Lieberman told the story of selling his company to a strategic acquirer and how he got more than ten times revenue for a nine-employee company. He did it by writing a software application that allowed brake manufacturers to catalog their various models. Michael dominated the brake manufacturing industry.

So when Autodesk decided they wanted to add product lifecycle management software to their lineup, they saw what Michael had done to corner the market and offered him a market-clearing price for his tiny company so they could stamp out his model in other product categories.

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PART 2

Emerging Acquirers

Hybrid Private Equity Groups

Don't be surprised if you haven't heard of hybrid private equity groups. They're a mashup of a traditional private equity group and a strategic acquirer. These acquirers specialize in buying companies in a specific industry, so you could make a case that they are actually hybrid.

Let's say a private equity group focuses exclusively on buying up small dental practices. Their objective is to buy small offices, roll them together, and take advantage of additional buying power for the supplies dentists need. The long-term goal is to sell the group down the road for a lot more than they paid for the individual parts. Technically, they are a private equity group, but in practice, they are acting more like a strategic acquirer.

Why bother considering an offer from a hybrid private equity group? Depending on your business, they could be the best of both worlds. Strategic acquirers tend to pay more than private equity groups but will likely want you to be an employee in a large bureaucratic environment, which can be soul crushing for a freewheeling entrepreneur. Private equity groups, on the other hand, may pay slightly less but will usually want you to remain in your business for a few years after you sell it. So if you're not quite ready to leave your company, a hybrid private equity group might be your ticket to a bigger payout while giving you the opportunity to continue operating your business.

SECRETS
to Negotiating with a Hybrid Private Equity Group

Get to know the Key Performance Indicators (KPIs) in your industry. (These are most often talked about at industry events.) Track your performance, and try to exceed the averages on each.

Inside the Mind of Business Owner Dr. Joseph Marchell and His Experience Selling to a Hybrid Private Equity Group

Dr. Joseph Marchell

In this episode of Built to Sell Radio, you'll meet Dr. Joseph Marchell and learn how he built his business in a way that was attractive to a hybrid private equity group.

In 2020 veterinarian Marchell started Old Brown Dog Veterinary Partners (OBDVP) after identifying a unique opportunity to do a rollup of family-owned animal hospitals.

Marchell acquired three practices for around ten times EBITDA. He then implemented a streamlined operational strategy that resulted in the sale of OBDVP less than two years later for almost three times the purchase price.

In the episode, you'll learn how to:

- De-risk your business for an acquirer.
- Create competitive tension in your company among acquirers.
- Utilize an audacious negotiation tactic to increase your offer.

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Acquisition Entrepreneurs

If you're getting emails from young MBA grads that want to buy your business, you've likely become a target of an acquisition entrepreneur. The rise of "entrepreneurship through acquisition" in top MBA programs signals a shift in career aspirations for business majors. Many graduates now prefer buying and building businesses over conventional career paths in consulting or finance. Their business model revolves around identifying businesses with perceived untapped potential, acquiring them, making strategic changes to improve performance, and realizing capital appreciation when they decide to exit.

They'll most often approach you backed by investors with whom they can co-invest and armed with fresh ideas and an eagerness to dive into entrepreneurship. The opportunity to apply their academic knowledge and practical skills in a real-world context fuels their passion for acquiring and managing companies. Moreover, the autonomy and control that come with owning and running a business appeal to their desire for independence and leadership.

In their pursuit of the right company to acquire, these entrepreneurs typically gravitate toward businesses with solid fundamentals that are underperforming relative to their potential in some way. They seek out businesses with clear growth prospects, stable cash flows, and opportunities to improve operations.

Ultimately, acquisition entrepreneurs most often target smaller companies because they're new grads and either don't or can't raise a lot of money to help support their acquisition goals.

SECRETS
to Negotiating with an Acquisition Entrepreneur

Make sure your company is bankable, and assure the acquisition entrepreneur (and their lender) that you'll stick around to help them in the transition with training and mentorship.

Inside the Mind of Acquisition Entrepreneur

Steve Divitkos

In his episode of Built to Sell Radio, Steve Divitkos, a Harvard MBA, detailed how he decided to acquire and build a small business using money he raised from investors. During the conversation, he revealed the pros and cons of selling to an acquisition entrepreneur.

In the episode, you'll learn how to:

- Avoid the most common reasons acquisitions fall apart.
- Structure the sale of your business to an acquisition entrepreneur.
- Avoid having to roll equity with your acquirer.

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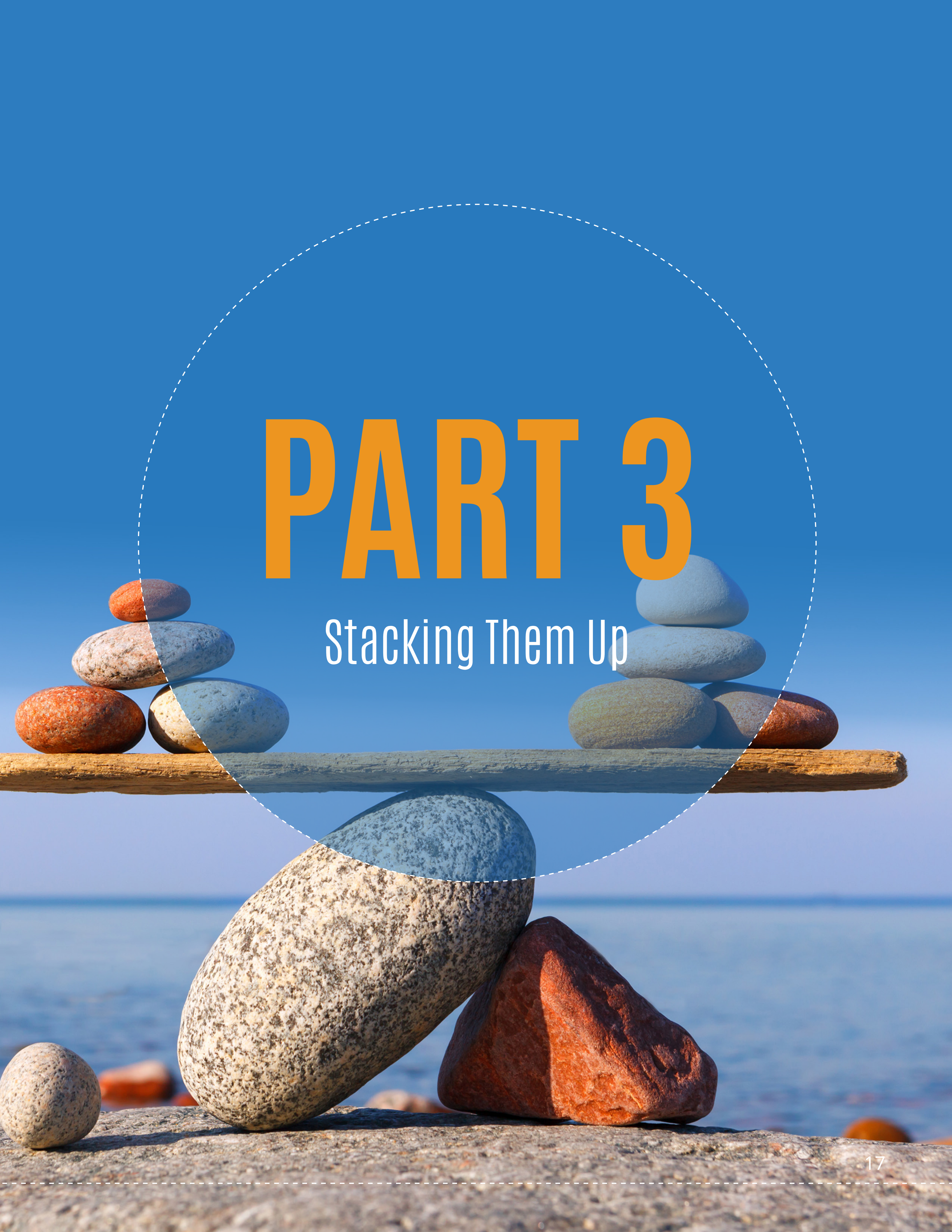
PART 3

Stacking Them Up



Every acquirer has its perks and drawbacks. Here's a quick guide to help you understand the different types of buyers and what to expect from each

	Pros	Cons
Individual Investor	• Typically this is a somewhat less sophisticated buyer, meaning diligence can be easier to pass	• A less sophisticated buyer who may damage your business/legacy • Might not be able to get financing to close • Pays the least • Often asks you to finance some of the deal • Buyers often get cold feet during the process
Private Equity Group	• Usually pays more than an individual investor • Very sophisticated buyer; will make sure business operates better and stronger • Often the equity you roll becomes worth a lot more down the road, which is referred to as "a second bite of the apple"	• Can be ruthless operators who may negatively impact your culture • Do not usually buy 100% and may ask you to roll equity • Use debt to acquire your business, which needs to be serviced, and that can put a drag on your operations
Strategic Acquirer	• Cleaner deals • Usually pays the highest price • Often allows the owner to leave quickly (unless it's a service business)	• Will most likely get rid of your name and brand • Bureaucratic and slow to make decisions • Diligence can take forever • Usually only buys larger companies
Hybrid Private Equity Group	• Pays well • High level of experience in your industry • Opportunity for you to stay on	• Will eliminate the jobs of your back-office employees (finance, HR, etc.)
Acquisition Acquirer	• New ideas and energy • Access to funds • Most want to honor your com pany name/legacy	• Will generally provide lower offers • Inexperience can lead to strategies that clash with culture • Limited practical experience

Conclusion

There's a range of potential acquirers out there, and each has their own reasons for buying and their own way of doing things.

An individual investor is often looking to buy a job. They may want the lifestyle benefits of owning a business and often have no plans to sell it.

Private equity groups can be mercenary acquirers.

Strategic acquirers are looking to make their business more valuable. They may not care about your business.

In addition to these traditional buyers, we're seeing new types of acquirers emerging, essentially remixing their best (and worst) qualities.

Selling your company is quite the journey. It's a mix of excitement, a bit of the unknown, and loads of potential. Just like gearing up for any adventure, selling your business takes some thinking and prep work. Getting a handle on who might be interested in buying and how they do things can really help make the whole selling process a lot smoother.