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Know your Buyers is a three-part series by Valitas Capital Partners for business owners. It is designed to help owners consider the types of buyers that are in the market, how those buyers perceive value, and the advantages and disadvantages associated with each. In previous instalments of the series, we discussed financial and strategic buyers. This month, we present different business scenarios and how the type of buyer impacts the outcome in each case.

Know your Buyers: Part 3

Christine Spence and Murray Brown own thriving commercial bakeries.

Both spent decades building their businesses from corner shops to the factories that house their current operations today.

Both generate healthy revenue and cashflow, at a level that might make their competitors envious.

Both are still working long, tough hours…maybe longer and tougher than they'd like (particularly in Murray's case).

And while both have adult kids, the kids have gone in different directions, and have no interest in the commercial bakery business.

Those are their similarities, and here are some critical differences…

Murray is 72 years old. He's tired of the long hours, and wants freedom to spend winters in the Florida sunshine, take up golf, and enjoy time with his grandkids. He's ready to realize the value from what he's built over the past decades and have someone else take over the business.

Christine just turned 60. This milestone birthday has triggered some thinking about how she wants to spend the next decade. Further thinking has been provoked by her long-time business partner, who recently announced that she wants to sell her 30% stake in Christine's bakery.

What will generate the most successful outcomes for Murray and Christine?

Murray

Murray is ready to sell. Unequivocally. He wants the best price that he can get for his business today, and is hoping to step out completely.

A strategic (corporate) buyer is likely the best option for Murray. This type of buyer will typically want to acquire 100% of the business, and offer the highest valuation because of potential synergies.

Competitive tension created through multiple bidders will generate the best price for Murray. To achieve this, he would be wise to retain an M&A advisor to manage the transaction process, as strategic buyers may have less M&A sophistication and a higher probability of leaking information. The right advisor will manage execution and confidentiality issues, and minimize Murray's exposure to these risks.

Christine

Christine isn't ready to retire just yet. She wants to exit in a few years time, but sees further growth opportunities in her business that she'd like to exploit first. Things are a bit complicated however, as she needs to find the capital to acquire her partner's 30% interest in the bakery, as well as to invest in future growth.

A financial buyer will be the best option for Christine. While this type of buyer would likely offer a lower valuation for her business than a strategic, the terms of an arrangement with a financial buyer will be more attractive to Christine. Management retention is important to a financial buyer, who will want Christine to retain an equity interest in her business. The financial buyer typically has a three to seven year investment horizon. At the end of that period, 100% of the business will be sold, most likely to a strategic buyer. Christine will benefit from the value creation in the business through her retained interest, and will be able to retire on a timeline that she is hoping for.

As in Murray's case, Christine would be wise to retain an M&A advisor to create competitive tension in the sale process, to negotiate the terms of the transaction, and to manage the process.

And they both lived happily ever after…

Murray

After entertaining multiple offers (brought to him by a trusted M&A advisor), Murray sold his business to a multinational bakery that wanted a platform to enter the Canadian market. He's currently living his dream and enjoying his grandkids…and he's seen huge improvement in his golf game.

Christine

Christine, supported by her M&A advisor, negotiated an attractive agreement with a financial buyer (a private equity fund). The buyer acquired 80% of the bakery, including the share of Christine's business partner. Christine retained a 20% interest, and continued to run the business for the next five years. During that period, the financial buyer provided capital for Christine to develop a new line of specialty breads that boosted the bakery's top and bottom lines beyond expectations. When it was time to exit, Christine sold her remaining 20% (alongside the financial buyer) for more than her initial transaction with the fund. She occasionally runs into Murray in Florida these days, though she prefers tennis to golf.