INSIGHT

A Shareholders Guide to Selling Businesses in the Middle Market:

The 8 Essential Principles To Getting the Best Price

Introduction

The subject of selling companies is inundated with information and instruction, but unfortunately, a significant portion of it lacks real-world deal-making experience. Consequently, it becomes challenging for business owners to make informed decisions and maximize their returns on the most important sale they will ever make.

At INSIGHT, we firmly believe that selling a company requires a proactive sales and marketing approach, and the eight principles outlined in these pages stem from that conviction.

These principles are not just theoretical but have been repeatedly tested and validated over our extensive history of selling companies in a significant number of industries.

Thank you for taking the time to read this, I trust that it will be beneficial to you as you consider the sale of your company.

James Kenward
Partner

Why Sell?

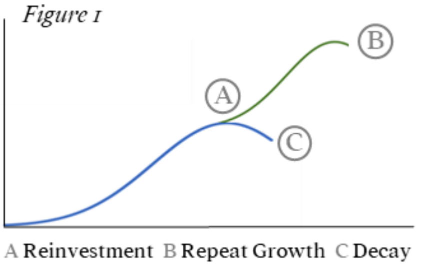
As a business owner, your decision to sell can be motivated by various factors. It is crucial to understand your objectives and motives because they will determine the shape and structure of your deal. Here are some of the typical reasons why owners choose to sell:

Change in Lifestyle: After spending many years in the business, some owners reach a point where they desire to pursue something different in life. It is normal for people to reevaluate their life goals every decade, so if your objectives are changing, you're not alone.

Entrepreneurs vs. Managers: Many owners of private businesses are entrepreneurs who are creative, full of ideas, and energetic. However, as the business grows, they find themselves increasingly held back by managerial responsibilities like employment legislation, personnel issues, health and safety matters, etc. They may feel that the excitement of running the business has gone, and a company sale becomes the logical and sensible way to exit and start a new chapter in life.

Time: The demands of running a business can be all-consuming, leaving little time for personal activities. This can be a significant reason why owners choose to sell their businesses, especially when it starts to affect their personal life.

Business Lifecycle: There comes a time when a sale is appropriate for both shareholders and the company. It may be due to the need for capital to grow the business, a merger with another company, or simply because it is the right time to exit. Many companies grow quickly in their early years (see Fig 1). In due course sales can start to plateau (A). It is often disproportionately difficult and expensive to break out of this plateau. A significant investment is usually required to hire key sales personnel, for new product development, or to implement a technology upgrade. If this investment is made, then the growth cycle could repeat itself (B). Without investment the company tends to decline (C).



A Reinvestment B Repeat Growth C Decay

For many business owners, their investment decisions are now a matter of inclination. They may have invested in the business for years, with the expectation that they would be able to start taking money out in the future. However, the thought of postponing the payoff or borrowing heavily to reinvest in the company is no longer a viable option. In such cases, a sale becomes the best option for both the company and shareholders. A new owner, most likely a larger company with vast resources, can help grow the business by leveraging its capital, know-how, clients, and distribution channels. This means that the company can continue to prosper, and shareholders can benefit from the sale.

The Essentials to Getting the Best Price

1. REMEMBER, THIS IS A SELLING ISSUE

Passivity is a significant obstacle to selling a private company. Many sellers view it as primarily a financial or legal issue and rely on their accountants or lawyers for guidance. However, these professionals may not have the necessary expertise to manage a comprehensive selling process and may only communicate with a handful of buyers, usually competitors. This limited approach is inadequate and fails to reach the entire pool of potential buyers.

It's important to recognize that selling a business is fundamentally a selling issue, not an accounting issue. Applying sales principles that you use for your products or services is equally essential when selling your company. Asking professional advisors, such as accountants, to sell your business for you may not be the best approach, as they may not possess the necessary skills and expertise to manage a successful sale.

It's also worth noting that the best buyers are usually not actively seeking to acquire new businesses. They may be successful and profitable but not currently looking for an acquisition. Therefore, it's essential to take a proactive approach and find them instead of waiting for them to find you. By applying effective sales strategies, you can increase your chances of finding the right buyer for your company.

2. BEWARE OF TRADITIONAL VALUATION METHODS

While traditional valuation methods tend to focus on short-term return on investment, such as valuing a company based on a multiple of its past profits, this approach overlooks future potential and assumes that past performance is the sole indicator of a company's value. At INSIGHT, we believe that this traditional thinking is fundamentally flawed.

To address this issue, we at INSIGHT use the "2x rule." To sell one company, we typically identify and communicate with a large number of buyers, a process that takes us around 2-3 months to qualify down to 5-10 serious candidates. Once we've reached this advanced stage of negotiation, we invite the candidates to submit competitive offers using our highly effective bidding process. Generally, we receive between 3 and 4 bids, with the lowest bid usually reflecting a traditional accounting valuation and the highest bid frequently being twice that amount.

At INSIGHT, we believe that this approach allows us to more accurately capture the true value of a company by taking into account both past performance and future potential. The 2x rule emphasizes the importance of thoroughly assessing a company's potential for growth and success and leveraging that information to secure the best possible outcome for our clients.

The Essentials to Getting the Best Price

Have you ever wondered why one company is willing to pay significantly more than another for the same business? The answer lies in a number of factors, including the establishment of a competitive bidding environment, the ability to sell future opportunities, and the motivations driving a buyer's decision to purchase a particular company.

Despite what some may claim, valuing a business is not as simple as applying a multiple to past profits. True value is determined by the motives of potential buyers and what the business will look like under new ownership. This means that it is never wise to attach a specific value to your company before taking it to market. In fact, doing so can be a costly mistake and one that is all too common in our industry.

At INSIGHT, we understand the importance of carefully considering all relevant factors when selling a business, from the motivations of potential buyers to the opportunities for future growth and success. Our approach emphasizes the importance of creating a competitive bidding environment that allows us to capture the true value of a company and secure the best possible outcome for our clients.

3. SELL THE FUTURE

Remember, a buyer is not interested in your company's past. They're only interested in its future potential.

What will your business look like once the buyer applies their financial resources, sales skills, and efficiencies? The best buyer is usually complementary, meaning they can promote your products and services to their clients and vice versa - this creates leverage points in negotiations.

So, when you sell your company, you should never sell what it looked like last year or what it will look like next year or in three years under your ownership. Instead, focus on what your business will look like under new ownership, with fresh investment, energy, ideas, and enthusiasm. This is what buyers are interested in, and this is what will help you achieve the best possible deal.

4. CHOICE IS KING

The most critical factor in selling a company is having multiple buyers to choose from. This factor surpasses all other considerations.

The presence of competitive bidding environment has a significant impact not only on increasing the price but also on maintaining it. If a buyer is aware that there are other buyers vying for the same company, they will be less likely to try and negotiate a lower price. This practice of reducing the price is commonly known as "price chipping". However, establishing competition among buyers is often the most overlooked aspect of traditional sales.

Moreover, having multiple buyers to choose from also expedites the sale process and gives you greater control over the terms of the deal. It is important to note that whoever has the ability to establish a choice of buyers holds the greatest control over the negotiation.

Therefore, lacking the option to choose can be detrimental to your negotiating power.

5. LOOK BEYOND THE OBVIOUS

If you limit your search for a buyer to only the most obvious candidates, you may miss out on better opportunities. It is essential to expand your search and consider potential acquirers outside of your industry, rather than just focusing on competitors.

Surprisingly, some of the best buyers come from unexpected places. Typically, your ideal buyer will be complementary to your business, rather than a direct competitor. Their products and services will likely complement yours rather than compete with them. What is crucial is that you share a customer base. In fact, most of the deals we facilitate involve complementary buyers who share customers with the seller.

The Essentials to Getting the Best Price

6. ALWAYS LOOK INTERNATIONALLY FOR A BUYER

It doesn’t matter how large or small your company is, to fail to look overseas is another common and serious error.

An overseas buyer will often pay a premium price to secure a foothold in a new market, because the purchase of an overseas business can require less investment and be executed significantly more quickly than building from the ground up.

Even if you end up selling to a local company (which is reasonably likely) the fact that they are competing with international bidders could have a profound impact on the bidding process.

7. BE PREPARED FOR THE COMING NEGOTIATIONS

Negotiation is where deals are made or broken. It requires asking the right questions, anticipating objections, thinking on your feet, maintaining control, and avoiding pitfalls.

Unfortunately, even knowledgeable advisors can be poor negotiators, and business owners can make matters worse. That's why we highly recommend negotiation training early on in the process. At INSIGHT, we take our clients through a negotiation training meeting to prepare them for potential negotiations with us and potential acquirers. While we handle negotiations on behalf of our clients, there may still be times when direct discussions occur. A little preparation can make a big difference in securing a good deal.

The Essentials to Getting the Best Price

8. FOLLOW A PROCESS

Preparation puts you in control of negotiations and avoids the delays and surprises that kill a deal. For those reasons, you should define and follow a comprehensive process from the beginning. Our process for selling a company has the following stages:

A. Preparation
Gathering all of the information required to undertake the project, consisting of:

- A total review of your own company and how you present yourself on social media
- Establishing all the benefits you have to offer
- Thorough financial preparation
- Considering future opportunities
- Market analysis
- Assessing the nature of possible buyers

Production of all documentation, including a Confidential Information Memorandum, forward-looking business plan, management presentations, financials (past and projected), and more.

Preparation for the upcoming face-to-face meetings with potential buyers

B. Research
Exhaustive research to identify potential acquirers both domestic and abroad, inside and outside of your sector.

C. Live to Market
A prospect generation effort of hundreds of phone calls, presenting the opportunity to senior business owners in a completely confidential manner. Careful assessment and analysis of the feedback we receive from potential buyers.

D. Deal Making
First in-person meetings with potential buyers, to provide additional detail on your business, discuss the potential combination benefits, and directly assess the quality and fit of each potential buyer.

Manage the bidding process in a way that leverages choice and maximizes price.

Work with an experienced transactional attorney to manage the due diligence and legal matters. During this stage you must continue to maintain choice as it has a profound impact on the speed of the deal and, therefore, the likelihood of completion.

INSIGHT

Discuss your business, its potential suitability for a sale transaction and the options available to you at an individual consultation with a senior INSIGHT partner. You'll be able to discuss your position in complete confidence, and meetings can be arranged at a time and location convenient to you.

To schedule, email contact@insightcf.com

COMPANY DETAILS

167 – 169 Great Portland Street,
5th Floor, London, W1W 5PF

contact@insightcf.com
www.insightcf.com