



THE SELLER EXPERIENCE

WHY OWNERS GET PREMIUM VALUES



EDGEPOINT

M&A
Advisory

RESULTS *with*
INTEGRITY™

INTRODUCTION

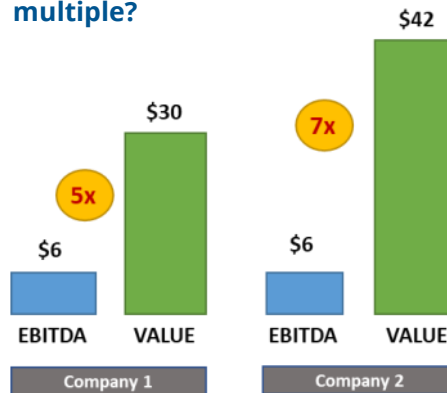
Attractive companies earn premium values.

Simply put, a company's value can be increased by raising earnings (EBITDA) or by meriting a larger purchase multiple.

This white paper will not attempt to address how to improve your business, operations and earnings. Instead, we want to address "Why some companies get paid higher multiples".

The graph below highlights two similar companies operating in the same industry.

Why did one company receive a premium purchase price multiple?



The transition/sale process is a singularly daunting, time-intensive and complex trek. And, for most sellers it is a once-in-a-lifetime event.

Wouldn't it be helpful to know what experience has taught others – to create the most successful outcome? That's the purpose of *The Seller Experience* whitepaper series – guidance from EdgePoint.

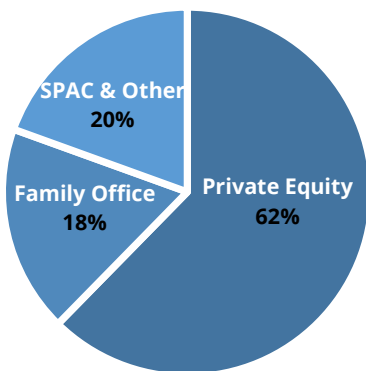
EdgePoint Survey: Buyer's Perspective on Company Attractiveness



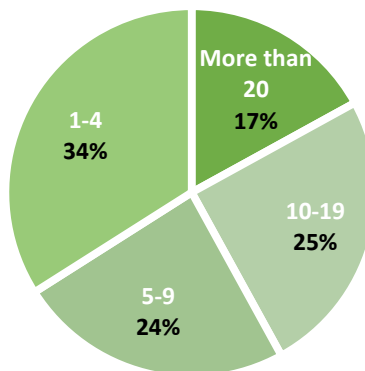
Information about what factors a buyer considers to arrive at a valuation multiple for a middle market business is limited. To gain insight, we commissioned an EdgePoint Survey: *Buyer's Perspective on Company Attractiveness*, conducted in January 2021. We asked **200 highly-regarded serial acquirers** of such businesses (private equity firms, family offices, SPACs and other financial buyers) to share their perspective, insight and experience. Their responses are the foundation for this white paper.

When we began the survey, we expected a few attributes to be highly-valued by these professional business buyers. We were surprised to see the diversity of responses from the respondents. The buyers surveyed were diverse in fund structure, geography, and investment objectives. Here are a few of the demographics of those surveyed:

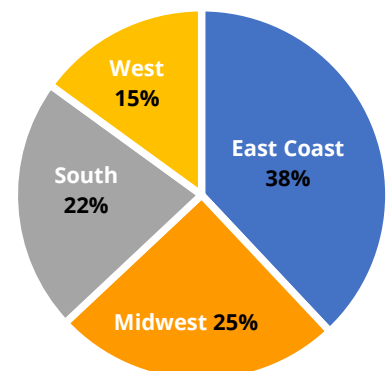
Buyer's Perspective Survey Participant Demographics



BUYER TYPE



LAST 3 YEARS ACQUISITIONS



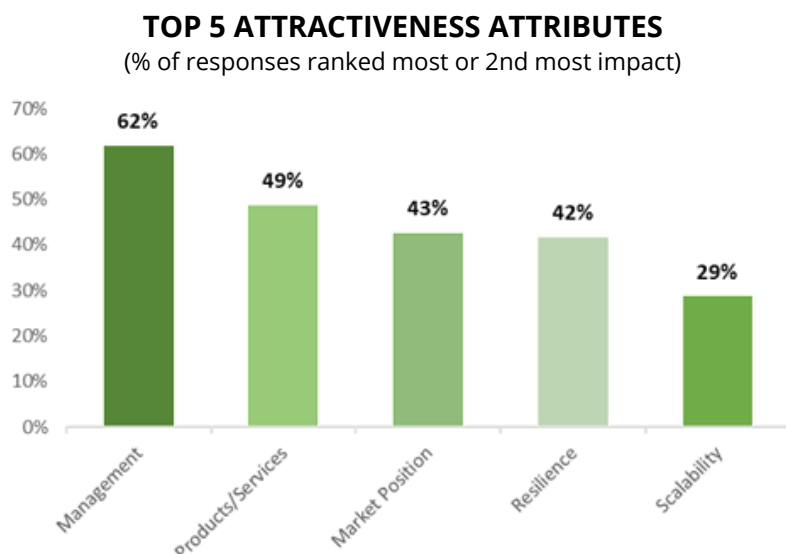
BUYER LOCATION

MAXIMIZE ATTRACTIVENESS

Professional Business Buyers' Perspective

Attractiveness, like beauty, is in the eye of the beholder. Buyers prioritize the attributes they seek, based on their strategies and skill sets. The diversity of responses for the most valued element was surprising. However, the top five most valued elements by professional buyers were clear. Overwhelmingly, the professional buyers we surveyed indicated that **these five attributes were highly valued.**

- **Strong Management Team** — The presence of strong, skilled and proven leaders that are willing and capable of growing the business in the future was the most highly valued characteristic. Owners that have invested in talent are often rewarded with premium values.
- **Differentiated Products or Services** — A unique product or service that has intellectual property or a prominent brand is highly valued by buyers. Similarly, if customers view the company's products/services as unique or 'must have' they tend to pay a premium price.
- **Strong Market Position** — A dominant position in a niche market or unique capability that provides differentiation is a characteristic of a highly valued business. The attractiveness of these end markets are often evaluated on their expected growth.
- **Resilience in Recessions, New Technology Threats** — Buyers and lenders value consistency of historical performance. Customers with long-term contracts or proven recurring revenue provide stability. The ability to weather recessions with small performance swings provides comfort to those extending capital on deals.
- **Scalability of Business** — Buyers seek segments with proven and projected high growth rates, so a company's systems, processes and people are valuable to growth-oriented buyers. Owners that have invested in process and systems for scalability receive higher values.



We are interested in finding the **ONE** buyer that aligns with our company's mission and culture, and is willing to pay a premium price and terms. The *"needle in the haystack"*.

Business Owner

OTHER ATTRACTIVENESS ATTRIBUTES

- **Customer "Stickiness"** and relationship tenure
- **Revenue Growth:** history and prospects for future organic growth and available acquisitions that have been identified or are ready for action
- **Gross Margin and EBITDA Margin** profiles; strong profitability relative to the market
- **Owner Transition:** owner's willingness to provide reasonable and orderly timelines for transition

MAXIMIZE ATTRACTIVENESS

Strategic Buyers' Premium Pricing

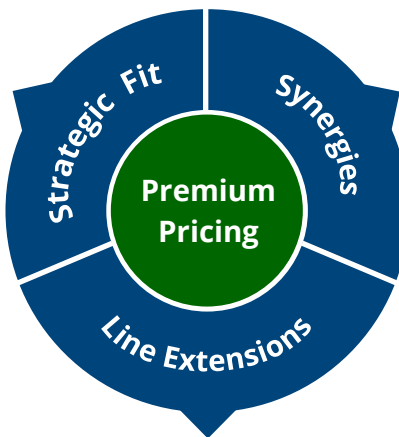
Strategic buyers are the ideal premium buyers. They have access to low cost capital, abundant operational synergies, and the ability to leverage an acquisition through their sales channels. These buyers value the same business characteristics as financial buyers, but they require a skilled banker to extract a fully premium value.

Over decades of M&A experience, we have determined that deals where strategic buyers pay premium values have the following **three core elements** overlaid on the attributes professional buyers seek:



Strategic Fit

Strategic buyers' corporate development departments have well-established strategic and acquisition plans. An investment banker with relationships and knowledge of their growth plans is invaluable. The development of a thoughtful acquisition thesis for each strategic buyer is essential to successfully court these premium buyers.



Synergies

The ability to reduce costs with volume pricing is just one example of synergies a strategic buyer can bring to the table. Sophisticated buyers tell us these synergies only occur with their acquisition, but an investment banker skilled at running a competitive process motivates a buyer to share these synergies in the form of a higher purchase price.

Product Line or Services Extensions

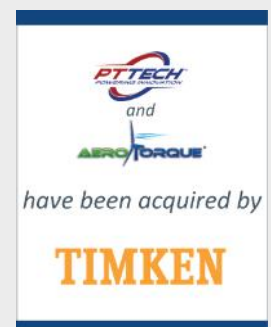
Strategic buyers often look for M&A opportunities to augment their existing products or services and complement their business plans. An investment banker with industry relationships and awareness of missing pieces can present the idea powerfully by proposing to fill product needs, geography gaps or talent shortages.

Strategic Buyer Case Study

PT Tech is a leader in advanced motion control and power transmission components for a range of harsh-environment applications. This R&D-focused engineered product company had made significant investments, but recessionary end-market pressures caused ownership to contemplate a sale of this highly valuable business.

PT Tech offered abundant synergies, a "must-have" addition to several buyers' product lines, and was a strategic priority for multiple suitors based on EdgePoint's industry knowledge. EdgePoint's approach to securing a premium market price included the following elements:

- Ability to quantify buyer's synergies and analyze the contribution margin
- Awareness of the strategic buyer's power transmission product lines and an understanding of the company's strategic acquisition interests
- Competition to ensure "FOMO: fear of missing out" which meant more money in the owner's pockets



THE INTERNATIONAL BUYER

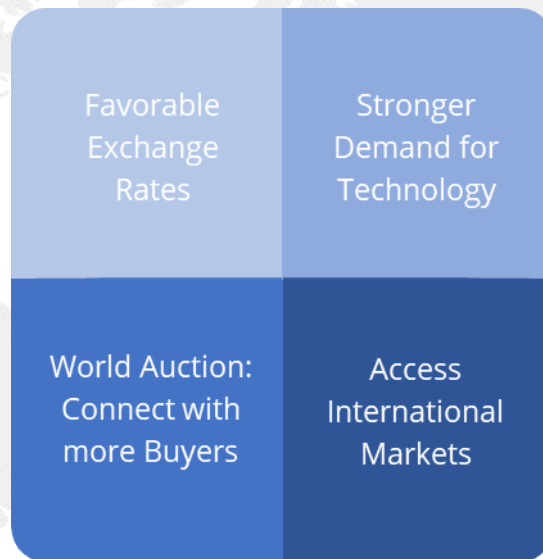
Access World Buyers to Maximize Value

The characteristics desired by financial buyers and the synergies offered by strategic buyers are potentially magnified even further with an international buyer. Selling products across borders greatly expands market reach and potentially allows for margin expansion.

The strategic rationales are more diverse and complex with cross-border buyers and should be considered to ensure that full value is received for your business.

Additionally, it is important that an investment banker have both cross-border experience and direct access to the decision-makers at these international buyers.

The following are the **top four rationales** noted for considering an international buyer



International Buyer Case Study

Nutricia, part of Paris-based food, beverage and nutrition company Danone, acquired Indiana based Real Food Blends, a niche specialty provider of real food meals for people with feeding tubes. Founded by a couple whose infant son needed a feeding tube, Real Food Blends is the only company that focuses solely on real food products in the \$1 billion U.S. tube-feeding market.

EdgePoint achieved a premium value and outcome from an international buyer as a result of many factors including:

- International buyer capable of expanding unique product that only enjoyed domestic distribution historically
- Buyer's superior access to capital enabled an all cash purchase price with low cost capital
- EdgePoint leveraged AICA alliance partner DDA & Company of Paris to smooth deal communications and negotiations.



MINIMIZE VALUE DETRACTORS

Beware of Concentrations and Other Major Risks

Sometimes value can be created by reducing those elements that decrease value. Buyers measure a company's attractiveness partly by the ABSENCE of **Value Detractors**. We asked our surveyed professional buyers about eleven of them and three were clearly at the top of their worry list:

- Customer Concentration** — Revenue concentrated with one or a few customers was the top value detractor. Respondents clarified that most would not purchase a business with customer concentration greater than 40% (concerned at 25%).
- Low or Declining Gross or EBITDA Margins** — Both gross margins and EBITDA margins (cash flow to service debt and growth) compared to other acquisition opportunities and the company's prior performance
- Cyclical or Declining Industry** — Negative industry trends greatly impact M&A demand and pricing. Owners operating in cyclical industries need additional planning and consideration on timing market cycles on an owner's transition.

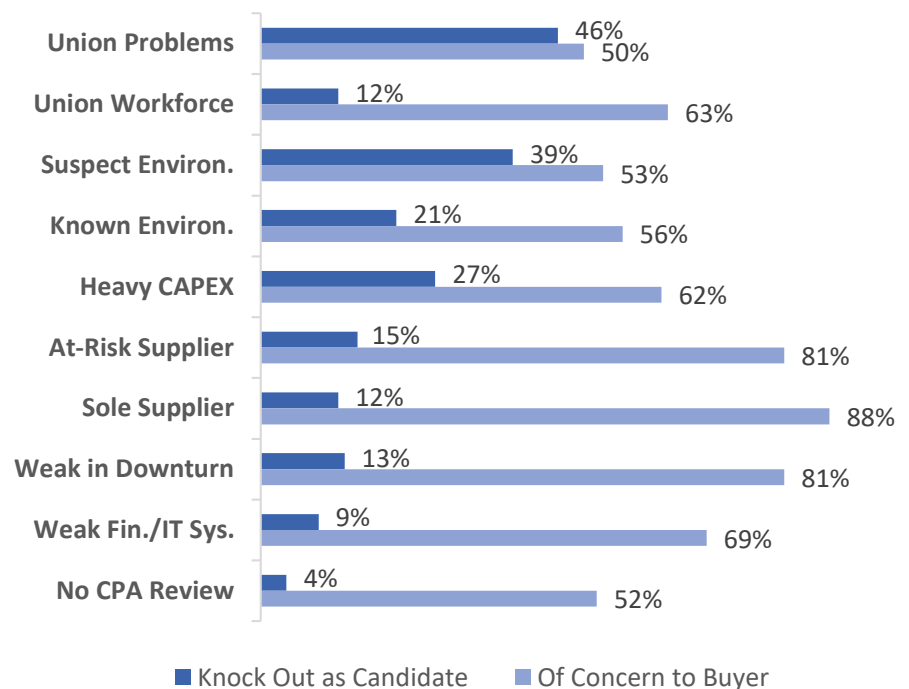
These other value detractors also concerned survey respondents:

- Union workforce**, especially if recent or anticipated problems
- Environmental issues**, especially if exposure is uncertain
- Heavy capital expenditures:** Outlays for equipment/working capital to continue growth, which most respondents defined as more than 5% of revenue or 20%-50% of EBITDA
- Supplier dependency:** Sole source for critical materials, parts or service or at-risk foreign sources

"Premium valuations occur when the risks are low and the certainty of success is high. A seller should focus on reducing the presence of risks."

EdgePoint Survey Respondent

VALUE DETRACTORS: KNOCK OUT OR CONCERN?



UNDERSTAND BUYER'S GROWTH PLAYBOOK

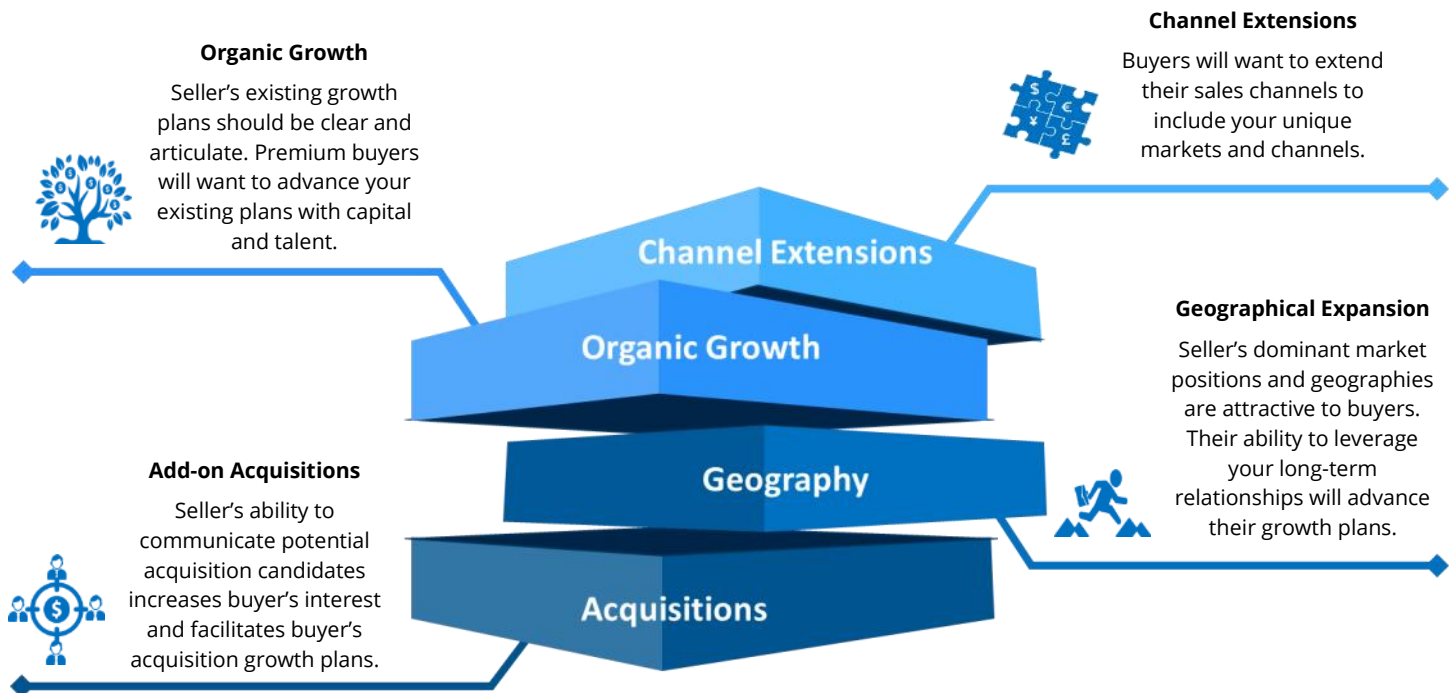
Growth Drives Premium Valuations

A key finding in EdgePoint's buyer survey was that confidence in the ability to grow the business is important to a buyer's willingness to pay a premium price.

For private equity buyers, the historical and projected growth rates are essential to receive a compelling valuation multiple.

The survey uncovered that most financial buyers surveyed determined that **attractive EBITDA growth rates are typically 10% a year or greater.**

The diagram below summarizes **factors driving premium valuations** for higher growth businesses. The ability to convince buyers of future growth requires the investment banker to be a skilled "story teller."



Private equity buyers value a compelling and credible acquisition growth strategy. The following three factors are important to supporting the acquisition strategy:

- Previous track record of completing and successfully integrating an acquisition
- Pipeline of potential acquisition candidates— Identified and contacted
- Proven management team, capable of integrating acquisitions effectively

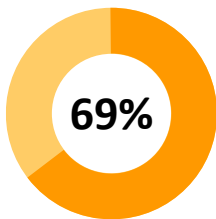
Most buyers' favorite questions to sellers were designed to understand the company's growth prospects, such as:

"If capital and resources were available, what would you do to double EBITDA in the next 3-4 years?"

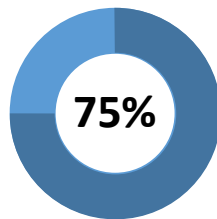
MONETIZE ATTRACTIVENESS THROUGH COMPETITION

Rely on the Right Advisors

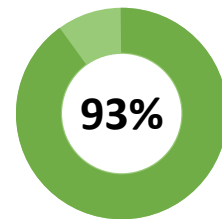
Professional buyers surveyed clearly stated they prefer to purchase companies represented by an investment banker even though they expect to pay a premium. To harvest a premium value in a tailored transaction, a well-orchestrated competitive sale process is necessary.



...of buyers prefer to have an **acquisition candidate represented** by an investment banker



...of buyers expect to pay a **higher purchase price** if the business is represented by an investment banker



...of buyers expect **higher certainty of close** if the business is represented by an investment banker

The conclusions reached from the EdgePoint survey augmented by decades of M&A transactional experiences are clear. Premium values are only achieved through competition, connected relationships with optimal buyers, and an investment banker's ability to convey your unique story. Sophisticated buyers expect a professional process with information easily available and are willing to pay a premium value for it.

About EdgePoint

Founded in 2000, EdgePoint is a leading independent national Merger & Acquisition advisory firm, specializing in middle market sale and ownership transitions, buy-side advice and innovative financing advisory services for business owners in the Industrials, Business Services, Consumer and Healthcare industries. EdgePoint is a FINRA-registered broker dealer, a member of SIPC and a member firm of the **Alliance of International Corporate Advisors**.

Our unique combination of large corporate finance expertise and deep middle-market knowledge gained through years of experience as entrepreneurs and seasoned advisors to midsize businesses provides our clients a high certainty of close. Our results have brought national recognition through industry awards.

Meet our team and learn more at www.edgepoint.com

