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Navigating the World of Mergers & Acquisitions

Tammie Miller, CFA

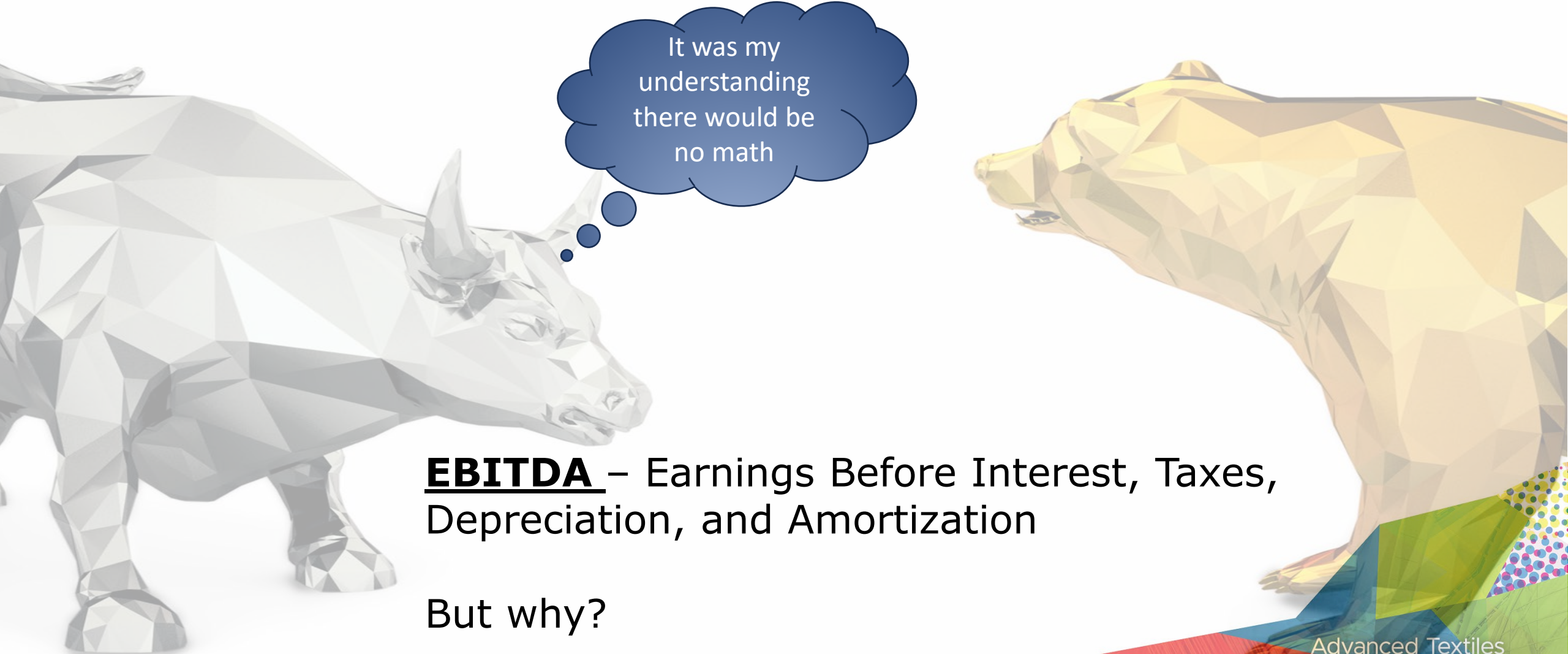


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About Me

- 25+ years in merger and acquisition advisory work
- Started on Wall St. at Lehman Brothers in New York
- Began career focusing on large corporate spin offs (think Richard Geer in *Pretty Woman* - **NOT** Julia Roberts)
- Have transitioned to a focus on family and founder owned businesses
- Predominately Sell Side Advisory
- Own my own firm, TKO Miller, with two other partners
- Based in Milwaukee – but we service clients nationwide
- Mostly transactions between \$10 million and \$250 million “lower middle market”

Some Terminology



It was my
understanding
there would be
no math

EBITDA – Earnings Before Interest, Taxes, Depreciation, and Amortization

But why?

Types of Buyers

Private Equity

Large pools of money generated by pension funds, university endowments, and insurance companies looking for higher returns. Generally, not open to small investors. Those funds are used, along with bank debt, to buy companies. Those companies are then sold within 3 to 7 years for a profit (hopefully).

Strategic

A buyer in the same industry as the target. They usually are looking to create synergies post-acquisition by eliminating redundancies between the two organizations – HR, Finance, overlapping factories, etc. Acquisitions can be to increase geographic reach, product line, or to eliminate competition.

Actual Names of PE Guys I Have Interacted With This Week

Private Equity Finance "Bros"



What's Happening In Middle Market M&A – Q3 2023

1.

We are one year into a sluggish M&A cycle with transaction and valuations down considerably.

2.

Data from all transactions shows that the average EBITDA multiple was 9.1x EBITDA in 2022 and is coming in at about 7.2x in 2023.

3.

4.

5.

What's Happening In Middle Market M&A – Q3 2023

1.

The bad news you keep hearing about in the news has largely been contained in the technology and consumer sectors, while many others have rebounded nicely.

2.

The middle market – in particular, the LOWER middle market – never really got hit at all.

3.

4.

Think about why families sell versus PE funds
Also – smaller transactions require less debt

5.

What's Happening In Middle Market M&A – Q3 2023

1.

2.

3.

4.

5.

Private Equity has gotten more selective about what they will acquire.

- Focusing on less debt-intensive add-on transactions
- Must be part of their investment thesis
- No last-minute surprises

What's Happening In Middle Market M&A – Q3 2023

1.

Economists expect the Fed to bring interest rates down.

That is usually followed by a decline in GDP and slow or NO growth in M&A.

M&A picks up historically the first quarter after Fed easing AND growth in GDP.

2.

- Fed cut rates in Sept. 2007 – no recovery until March of 2009

- Fed cut rates during pandemic April/May 2020 – making the data from the 2019 cut unreliable

3.

However – historical data is unclear as guidance because private equity was not the power player in the economy that it is today.

4.

Some perspective:

27% of M&A transactions with PE in 2007 vs 39% in 2022.

PE portfolio companies in the U.S. more than doubled between 2007 and 2022 to almost 11,000.

Dry powder in 2007 = \$700 billion vs \$1.7 trillion in 2022

5.

M&A Recovery is Going to Come More Swiftly

What's Happening In Middle Market M&A – Q3 2023

1.

We cannot ignore the population dynamics in the United States.

2.

There are approximately 350,000 lower middle market companies in the U.S., employing 30% of our workforce and generating about one third of the nation's GDP.

3.

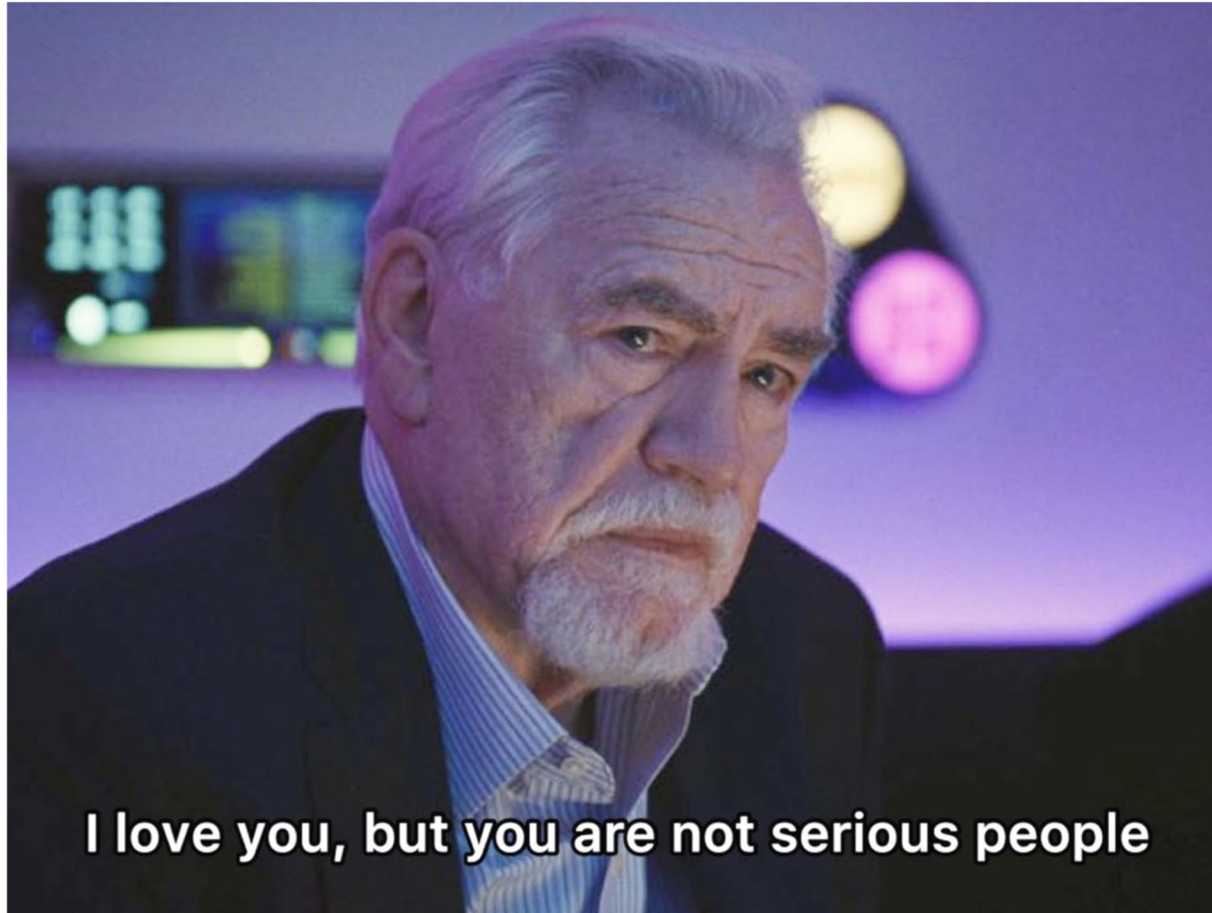
About 70% of these businesses will need to be sold in the next decade because their owners will need to retire, and they do not have exit plans.

4.

These sellers certainly aren't ignoring market factors but unlike professional private equity or strategic sellers, they aren't trying to time the market – they're trying to outrun Father Time.

5.

Family Businesses Are Unique



- Average life span of a family business is 24 years (*familybusinesscenter.com 2010*)
- About 40% of U.S. family-owned businesses transition to a second generation
- About 13% are passed down to a third generation successfully
- Only 3% survive to a fourth transfer or beyond (*Businessweek.com 2010*)

What If I Want to Exit?

Get Organized

People

Financials

Facilities/
Inventory/
Equipment



- Make sure the management team is solid and doesn't have any holes

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- Hire professional advisors – don't skimp – use specialists
 - Investment banker/business broker
 - M&A attorney
 - Accountant

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 - Investment banker/business broker (sell-side advisor)
 - M&A attorney
 - Accountant
- Think about stay pay arrangements for key people

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- Have at least three years of financials reviewed if you are not audited.

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- Think about potential “add-backs” to your business and document what those expenses might be. Discuss with your accountant and investment banker.

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- Think about potential “add-backs” to your business and document what those expenses might be. Discuss with your accountant and investment banker.
- Prepare a list of revenue by customer and look for any concentration issues that may need to be addressed.

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- Think about potential “add-backs” to your business and document what those expenses might be. Discuss with your accountant and investment banker.
- Prepare a list of revenue by customer and look for any concentration issues that may need to be addressed.
- Look for any other material changes in the financial statements and prepare explanations. Large customer losses? Changes in margins?

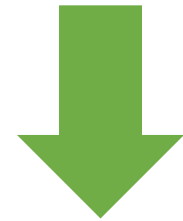
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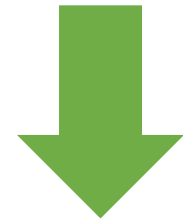
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- Make any necessary repairs or maintenance
- Write off obsolete inventory/clean up balance sheet

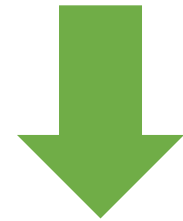
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- Organize (have available) all contracts (if applicable) with customers and suppliers

What If I Want to Exit?

Most Importantly – Run a Competitive Process!

What is that?

- Everyone receives the same information at the same time
 - Allows you to compare apples and apples
- There are multiple buyers
 - Buyer lists for lower middle market companies regularly include over 100 potential buyers
- Your company is positioned in the most positive light for potential buyers
- The process is run in a confidential manner
- There are clear milestones and timelines that all parties must meet

What Do Investment Bankers/M&A Advisors Do During the Sale?

1a

Prepare the Company Marketing Materials (4-6 weeks)

- The Offering Memorandum or Confidential Offering Presentation (CIP) is a 30 to 40 page deck laying out key information and metrics about your business at a very high level
 - Historical financials
 - Customer analysis
 - Product Information
 - Markets
 - Organizational Structure
- Teaser is a no name document sent to potential buyers to generate interest
- Data Room is an electronic repository for all company information and is generally not opened until later in the process

What Do Investment Bankers/M&A Advisors Do During the Sale?

1b

Create a Buyer List

- Collaborative effort along with business owner
- Discuss how to approach each potential buyer
- A good banker can bring buyers to the table through their knowledge of the sector and network

What Do Investment Bankers/M&A Advisors Do During the Sale?

2

Market the Company (4-8 weeks)

- Make initial contact with prospective buyers
- Put NDAs in places and send the CIP/Offering Memorandum out
- Qualify the buyers
- Receive first round bids (exciting day!)

3

Management Presentations (2-3 Weeks)

- Select top 6-8 groups to meet the management team
- Usually combined with facility/site visit
- Take about a half day each
- After all management presentations are complete, everyone has access to the data room and re-bids

4

Picking a Buyer & Due Diligence

- With more information and having met management, everyone has a chance to re-bid
- Following those bids, the Seller, with the help of the Investment Banker, pick a Buyer and move toward closing the transaction
- Due Diligence – very stressful
- Other management usually need to be made available

5

Negotiate Purchase Agreement & Close (8 to 12 weeks)

- This is a period of exclusivity (don't talk with anyone else)
- In reality, there are many small decisions here that can cost you money
- There are also many documents in addition to the purchase agreement that you will be discussing
- Run through the tape!

What If Someone Approaches Me With a Really REALLY Good Offer



This might be exciting, attractive, and potentially life-changing, but if you take anything away from today – take a moment to breathe and don't do anything.

When a team of advisors helps you to sell your business through a competitive process – it is called sell-side M&A.

How does buy-side M&A work?

- Dialing for dollars
- Seller isolation is key
- Eliminate competition

Frequently Asked Questions

Q: How long does a business sale take?

A: The sale process from the time you hire an investment banker or M&A advisor, to completion, can take 7 to 9 months. Usually, the last 60 days are active due diligence and negotiation.

Q: Post-sale, can I leave right away?

A: It is very unusual for a seller to be able to leave immediately after a sale is complete. In most transactions, a seller is required to stick around for some transition period.

Frequently Asked Questions

Q: How does it stay confidential?

A: A couple of ways:

- Limit the number of people involved
- Confidentiality agreements/NDAs
- Move quickly!

Q: What about my employees?

A: Think about stay-pay arrangements before you start a sale process for key people. Types of buyers can make a big difference. Remember – PE usually wants/needs everyone.

Frequently Asked Questions

Q: What was the strangest thing a client has done during a meeting with a potential buyer?

A: People get very nervous during management presentations. During one of these, a CEO took off his socks and shoes, brought his sock up to the table laid it flat and repeatedly “smoothed it out” during the meeting.

Q: What happens to the cash in my company?

A: Transactions are usually structured to be “cash free/debt free” meaning that the purchase price assumes that you keep the cash in the company, but you also must pay off any of its non-trade related debts.

THANK YOU



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