What Type of Buyer is Right for Your Company?

Different types of buyers have different objectives and levels of experience. Knowing these differences can help you in getting the deal you want.

As you begin your discussions with potential buyers, it's important to keep in mind that their goals and objectives can vary greatly. In general, buyers can be classified into three major categories: strategic companies (both public and private), Private Investment Groups, and individual investors.

Each buyer type presents a unique set of advantages and disadvantages that can have great impact on the ultimate outcome of the sale. Understanding these differences can help you, both in your negotiations and in finding the best buyer to meet your business and personal goals.

Strategic Companies
Acquisitions by strategic buyers are generally driven by potential synergies between the acquirer and the target entity. For example, you may have a product or service that the buyer lacks, but is highly complementary to their product or service offering. Or, you may have an established presence in a certain geographic or customer market that the acquirer has had difficulty penetrating.

This focus on synergistic value may result in higher offers from this buyer group than from others, since the operational efficiencies that are created can provide immediate higher profitability and a more rapid return on investment for the buyer.

Public and private strategic buyers differ in that the liquid market for public company shares may create a more aggressive valuation for public firms over those that are private. This may allow the publicly traded company to pay a premium price for your business, especially if you're willing to accept a stock-for-stock transaction.

The company structure after the sale may also differ with a sale to a strategic buyer. For instance, unless management is viewed as absolutely critical to maintaining company performance, these buyers generally don't require that the active, selling shareholders remain with the company much past a short transition period (generally six months to a year). Also, depending upon the size of the target and the logistics involved, the buyer will oftentimes completely absorb the target company into its current operations, making the ability to relocate the target company an important consideration.

An additional consideration for strategic buyers is the clarity of historical corporate records. Large buyers are particularly sensitive to possible liabilities (licensing issues, outstanding contracts, taxes, etc.) that they may become liable for upon purchase. Therefore, as is the case with virtually all transactions, it's recommended that any outstanding issues be clarified prior to discussions with a strategic buyer.

The advantages of dealing with a strategic buyer include:

- Their expertise in closing transactions often expedites the closing
- They generally have a wider range of deal structure and financing options than other buyer segments
- They usually have sufficient resources (both financial and otherwise) to support company expansion and growth

Possible disadvantages include:

- Absorption of the seller's operations into the buyer's operations may be required
- Contingent payments, that depend upon the tracking of financial performance, may be harder to monitor because of the difficulty of keeping separate records
- Some employee positions may be eliminated due to consolidation of operations or elimination of back office functions
- There is often a resultant change in corporate culture

Private Investment Groups (also known as Private Equity Groups)

Private Investment Groups represent a formal fund (or a number of related funds) created by a group of investors for investment in, and purchase of, closely held businesses.

The strategy and focus of these groups varies widely. Some groups focus on a certain industry segment, while others are more concerned with the geographic location of the target. Certain investment groups may achieve the same synergies with an acquisition as corporate buyers, particularly if the group is building a portfolio of businesses within a specific industry. In any case, the Private Investment Group's primary focus is to achieve the highest possible financial return for its investors.

Since investment groups generally prefer to let their portfolio companies continue to operate on their own, the preference is for the existing management team to remain after the sale. Additionally, these groups usually have a planned exit strategy and expect to hold a portfolio business for a pre-determined period of time - usually between five and seven years.

The advantages of working with an investment group include:

- With professional buyers the closing of the transaction is often expedited
- They often provide access to resources the seller may not have (managerial talent, financing, etc.)
- Their equity capital has usually already been raised
- The acquired company generally experiences little culture change

Possible disadvantages include:

- The requirement for management to stay may conflict with the shareholders' exit plans
- The transaction may not offer synergies with other portfolio businesses
- As cash flow-oriented buyers, these groups usually pay a fair but not premium price for the businesses they acquire
- The company may face being sold again within five to seven years

Individual Investors

Individual investors are high net worth individuals seeking to own and manage their own company. Individual buyers expect to be integrally involved in the leadership and management of the company after their purchase. This buyer segment is usually more focused upon the geographic location of the target than its industry, as the buyer is typically not seeking to relocate.

Most individual investors are seasoned businesspeople, with experience in either corporate positions or other entrepreneurial ventures and ordinarily prefer established businesses with proven performance to newly started companies. Due to capital constraints, individual investors usually purchase businesses at the smaller end of the middle market spectrum.

The advantages of working with an individual investor include:

- They'll have direct involvement, and therefore a stake in the success of the business
- They generally only require active shareholders to remain for a short transition period
- They're usually not seeking to relocate the business or drastically change operations and culture

Possible disadvantages include:

- They're typically inexperienced in purchasing businesses, which may prolong negotiations
- Their financing and deal structure options are normally not as broad as with other buyer segments
- They're not as likely to pay a premium price for the business
- They may not have direct industry expertise

Keep in mind that the payment portion of a buyer's offer should not be your only focus in a transaction. Your understanding of the buyer's ultimate plans for the business, their expected level of involvement and network of resources, are all important considerations. Knowledge of a buyer's expectations for the business can be highly beneficial for both negotiations and the closing of a successful deal.

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