Selling Your Business – Separating Myth from Reality and the Importance of Hiring an Experienced Investment Banker

You may have heard the saying 'you don't walk into a courtroom without a lawyer.' If you have legal issues and you're not a lawyer, you're likely to hire an attorney that specializes in the area of law relevant to your issue at hand. Likewise, you probably have an experienced accountant to prepare your business's tax filings, given the complexities of the tax code and the implications of not having your taxes done correctly or on time. There should be little doubt then, that when you decide to sell your business (likely one of the most important financial decisions of your personal and professional life), you should consider hiring an advisor who has the experience to guide you through a process about which you may be somewhat familiar, but do not have the in-depth knowledge or the time available to manage on your own.

What exactly does an investment banker do to help you sell your business and how do they add value in this process? You may readily understand how a lawyer or accountant can help you when you seek their services – but what about an investment banker?

One of the first ways that an investment banker can advise you as you contemplate selling your business is with regard to value: What is your business worth?

> **MYTH:**
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> **"I MET WITH A HANDFUL OF INVESTMENT BANKERS AND NOW KNOW WHAT MY COMPANY IS WORTH AND HOW LONG IT WILL TAKE TO SELL."**
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> **REALITY:**
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> Initial estimates regarding value are not offers. Further, as in every industry, there are unscrupulous investment bankers who will tell you your business is worth a lot more than it is in order to get hired. Your business is worth what a buyer is willing to pay and can only be realized through a competitive sale process, which takes time and requires significant negotiation. With regard to the time it takes to sell your business, of the most recent sales transactions completed by HighBank:
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> - *The average time from <u>signed engagement</u> to close was approximately 9 months.*
> - *The average time from <u>going into market</u>* to close was approximately 7 months.*
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> * The 2-3 months that it takes to get a company "in market" is indicative of the extensive process needed to properly prepare a company for sale.

Before initiating a sale process it is critical to receive expert and objective input on how your company would be valued by a financial or strategic buyer. An experienced – and active! – investment banker will be up-to-date on M&A trends, relevant public market and transaction multiples in your industry, and may have proprietary intelligence about recently completed transactions. When interviewing an investment banker you should expect them to provide you with initial valuation guidance. This will allow you to determine if your value expectations are realistic, and ultimately this information may (or may not) compel you to proceed with the sale of your business. The guidance received in these initial conversations with an investment banker, however, is just that – an estimated range of what a buyer is likely to pay for your business based on historical information and current market conditions. Different investment bankers may present you with varying value ranges and you may feel compelled to select the advisor that indicates the highest value for your business. Do not, however, let this be the deciding factor. Maintaining realistic value expectations is critical when you undertake the sale of your business as this establishes the parameters under which you are actually willing to complete a transaction; any investment banker that unrealistically inflates value expectations to win your business is not doing you any favors.

Ultimately, the "real" value of your business will be determined through a much more detailed analysis of your business and the undertaking of a competitive sale process. This is when the importance of hiring an investment banker is realized. You can gain a general sense of how much your business is worth by interviewing a handful of investment bankers; but the most compelling reason to ***hire*** an investment banker is to ensure you have an advisor that has the expertise to best position your company for maximum interest, the skills and resources to run a competitive process, an ability to structure the economic aspects of the deal, and the proven (through former client references) negotiating finesse to complete the sale on the most attractive terms.

MYTH:

"I CAN SELL MY BUSINESS ON MY OWN."

REALITY:

You can, but you're less likely to realize the full value of your business. We polled 10 private equity (PE) firms active in the middle market and the benefits of having an investment banker advisor are evident:

- *Percentage of investments made in a competitive process: 76%.*
- *Estimated premium paid in a competitive process: increase of 1x EBITDA (with answers ranging from 0.5x to 2x increase in EBITDA, all positive!).*
- *Percentage of transactions where PE firms hired an investment banker when exiting their own portfolio company investments: 94%.*
- *Extent to which an investment banker makes the due diligence process run more smoothly for the seller and*

The figure below summarizes how an investment banker adds value at each stage of the sale process.

Key Highlights of How an Investment Banker Adds Value during a Sale Process
Stage 1: Develops a "Go-to-Market" Plan
♦ Assembles a thoughtful list of potential buyers that includes the logical strategic acquirers and the financial firms with demonstrated interest in the industry, as well as the "outside-of-the-box" companies that could place significant value on your business. ♦ Creates compelling marketing materials that best position your business to potential buyers; tailors as needed to each buyer to create a compelling story. ♦ Establishes and manages a secure data room that allows for efficient access to company information. ♦ Provides updated valuation guidance to properly set your expectations.
STAGE 2: Creates a Competitive Sale Process
♦ Generates interest among buyers through high-level conversations based on each potential acquirer's specific acquisition history, publicly communicated strategic initiatives, existing "gaps" in products and services, etc. ♦ Drives deal momentum by soliciting indications of interest (including preliminary value indications) from potential buyers, which serves to differentiate interest levels between potential counterparties. ♦ Provides expert coaching to business owners to prepare for management meetings with selected parties and helps position the business for the best possible valuation. ♦ Assists in selecting the most interested and "best-fit" potential buyers for continued discussions.

STAGE 3: Selects a Buyer and Structures the Transaction
♦ Creates a competitive environment amongst final bidders by negotiating with multiple potential buyers until it becomes clear that the best offers have been put forth. ♦ Prepares comparative information on final offers to a business owner to assist in evaluating and selecting the "best-fit" buyer; this includes a detailed assessment of purchase price as well as other key factors (the "best-fit" buyer is not necessarily the bidder that puts forth the highest valuation). ♦ Advises on the structure of the deal and negotiates key seller-friendly terms with the selected acquirer prior to the signing of a letter of intent (which typically grants exclusive rights to the selected acquirer) in order to maintain the seller's negotiating position.
STAGE 4: Completes Negotiations and Closes the Deal!
♦ Manages the extensive due diligence process by responding to the selected buyer's requests for information and updating the data room. ♦ Negotiates final deal terms in a time-efficient manner, reducing costly "back and forth" document reviews. ♦ Coordinates with legal advisors on business terms and documentation to finalize the purchase agreement.

In addition to the information summarized in the figure above, there are some additional factors to consider if you still need to be convinced of the value in hiring an investment banker.

Time is money. Selling your business can be a daunting and time consuming undertaking. It typically takes over six months to complete a transaction. One of the primary objectives for an investment banker is to drive the process and keep the deal "on track" while you focus on what you do best – running your business. Maintaining business performance during the sale process is critical to achieving maximum value.

Don't let your emotions get the best of you. Selling your business can be an emotional endeavor. There will be times throughout the process when the scrutiny from potential buyers can feel like a personal affront, when in actuality it is just a normal part of the due diligence and negotiating process. Further, these emotions can lead you to forget the objectives you had in mind when you started the sale process. An experienced investment banker serves as a thoughtful sounding board that will not only advocate for your best interests but keep you grounded and realistic.

MYTH:

"I HAVE OFFERS FROM BUYERS EVERY WEEK, WHY WOULD I HIRE AN INVESTMENT BANKER IF BUYERS ARE COMING TO ME?"

REALITY:

These are not offers they are inquiries. An experienced investment banker will possess the skills to "weed out" those parties who are not truly interested or capable of consummating an acquisition or who may just be "bottom fishing." Your investment banker should:

- *Leverage market insight and research capabilities to include "less-than-obvious" potential buyers in the process, which will increase the number of interested parties and in turn increases value. In some cases, an initially unforeseen counter-party is the ultimate buyer.*
- *Negotiate an increase in the purchase price above what was initially submitted in the letter of intent; in the most recent sales transactions completed by HighBank,* ***valuation, on average, increased approximately 12% from the initial letter of intent submitted by the winning bidder to the final signed letter of intent****.*
- *Ensure seller-friendly terms that may not directly impact the at close purchase price but will reduce post-closing risks.*

The devil is in the details. Throughout each stage of the sale process (as summarized in the figure above) there are layers of minutiae. An investment banker not only develops and drives the high-level strategy of a competitive sale process, but drills down into the many details that are inherent at every stage of the sale process; this includes wrangling volumes of information into concise marketing materials, finalizing a multi-faceted valuation analysis, summarizing and presenting a summary of the relevant terms of the purchase agreement in a comprehensible and meaningful format, as well as focusing on the nuances in relationship-building with a potential buyer. (The second article in this series, "Selling Your Business – Eight Things a Buyer Will Want to Know," provides additional insight into the level of detail required during the marketing and due diligence stages of the sale process.)

Selling a business is a complex process and is as much a science as it is an art. Like any "specialty" advisor, an investment banker not only must have the requisite technical skills, but must also bring an expertise honed through years of experience and the cumulative knowledge gained only through completing numerous transactions. Don't believe the myths about selling your business. Hire an advisor with the experience and expertise to achieve an outcome that will meet your sale objectives.