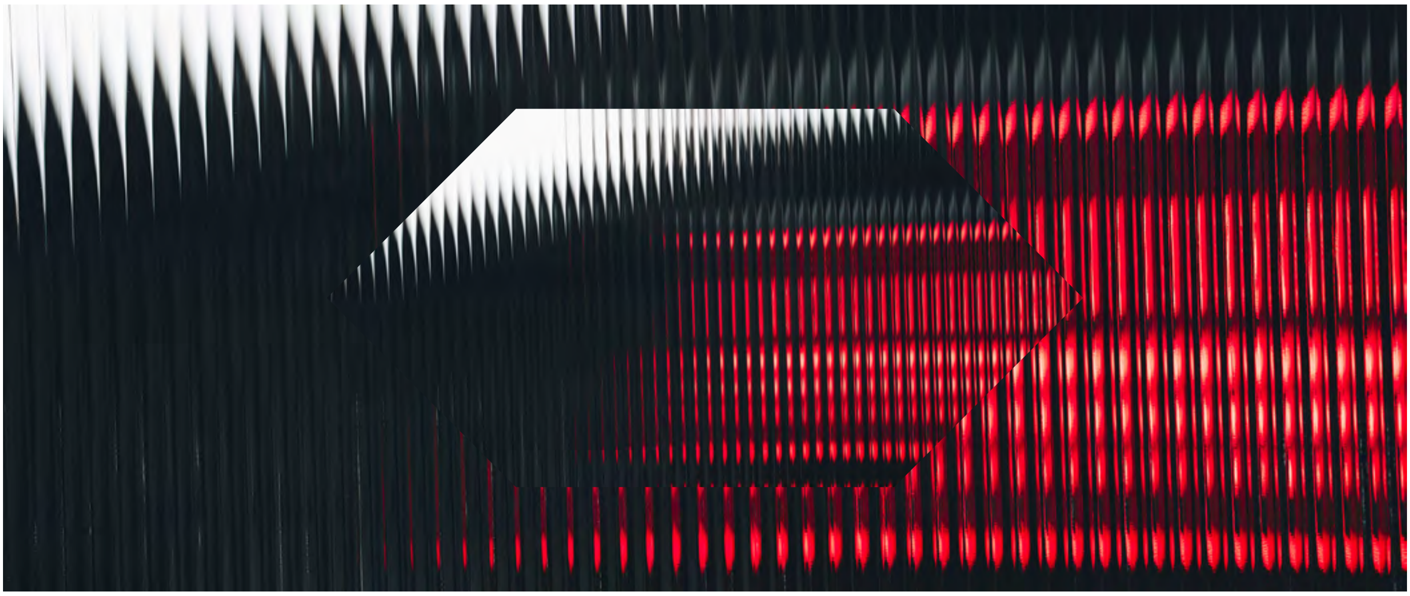
Beyond Business Ownership: Understanding the Buyer Universe



For sellers of businesses the Buyer Universe can be complex. It consists of parties inside your business – such as management or employees – and external entities, such as private equity firms, family offices, trade buyers and more. When it comes to selling your business, it's important to understand which type of buyer might be the best fit for you and your business and how to engage accordingly.

Key takeaways:

- Start by understanding your motivations for selling and what you hope to achieve for the business and your financial future – this can influence your buyer selection process
- Use professional advisors – their expertise can help shed light on appropriate choices for the sale
- Consider how to ready your business for a sale – this can start several years before you intend to exit, and should bear the potential buyer type in mind.

Understanding internal buyers

Internal buyers are parties within an existing company seeking to purchase the business. The sale could be in the form of a management buyout, an employee ownership trust (EOT), or a family buyer wishing to take over the business. But what makes each internal buyer type different?

1. **Management buyouts, organised by management teams, can be an ideal option if you're keen to see the business continue to flourish when you exit.**

"A sale to your management team might appeal if you are looking for peace of mind when exiting your business," explains Russell Prior, Managing Director and Regional Head of Family Governance, Family Office Advisory & Philanthropy, HSBC Private Banking in EMEA.

Implication on value: Management buyouts may offer reduced value but can bring additional benefits. "A management buyout may offer a lower valuation but might ensure continuity and a smoother transition, similar to other internal buyers, such as employee ownership trusts and family buyers," says Alisdair Hillis, Senior Director – Finance Sponsors Coverage, HSBC UK.

2. **Employee ownership trusts (EOTs), vehicles that allow employees to take ownership of a company, can offer more employee engagement, retention and increased morale.**

While management team buyers may seek to exit the business within a certain timeframe, EOTs provide a greater continuity of ownership.

"When selling to an EOT, it's important to have a good internal culture that will continue to benefit employees on a long-term basis," says Susie Mullin, Partner, Blick Rothenberg.

EOTs can benefit all employees. "They [founders and shareholders] are selling to people they've normally hired themselves, and they're looking after those employees and giving back," says Peter Golden, Head of Tax and Private Client, Fieldfisher.

Implication on value: Improved morale amongst employees can contribute to a thriving business to carry your business legacy forward.

3. **Family buyers are likely to encounter an emotional dimension to their decision-making – both parties will want the best deal for themselves, while protecting the family relationship.**

"Going forwards, [family members] normally have a relationship together. Emotion is therefore involved in trying to achieve the best terms, and negotiating the types of contracts and warranties which are required in a sale," Golden points out.

Implication on value: Selling to your family can be an emotional process, however it can help different generations obtain what they need "Maybe with an older generation, they might consider taking some value off the table," explains Mike Tillson, Partner Corporate Finance, Grant Thornton UK LLP.

Understanding external buyers

External buyers include trade buyers, private equity (PE) buyers, family offices, and initial public offerings (IPOs). Each brings a different dimension to a sale. To help decide what's right for you, start by defining your goals to identify buyers who align with your strategy.

1. **Trade/strategic buyers typically see the value in the transaction and understand the business they're looking to acquire because they tend to operate in the same sector.**

"Trade buyers are often looking to strengthen their position or expand their presence within the market, diversify their product or service offering, or create synergies to improve their operations," says Andra Ilie, Senior Adviser, Family Governance, Family Office Advisory & Philanthropy, HSBC Private Banking in EMEA.

"They are typically seeking to gain synergies, expand in the market, or secure technological advancements, believing the combined entities will be stronger together," says Hillis. "For example, a strategic buyer could be looking to acquire a company that enhances their own value, such as a tech business looking for a particular kind of tech that they don't already have," adds Mullin.

While the after-sale transition may be smoother, it's worth considering whether the organisational implications align with your preferred outlook for the business and its employees. "Their familiarity with the sector gives trade buyers a greater clarity of purpose and potentially better terms and value, however they may seek to integrate the business into their existing operations," adds Prior.

Implication on value: By understanding the market, trade buyers can be in a better position in terms of seizing the opportunity and extracting value from it. "Business owners may choose to go for a sale on the basis of getting better terms and potentially better value," says Golden.

2. **PE buyers offer the potential to scale quickly, gain access to capital and expertise, and the opportunity to retain a stake in the business.**

PE buyers are typically more interested in growth potential and delivering financial returns than other types of buyers, and often hold investments for three to seven years before exiting. "PE firms invest in businesses with strong cash flows, aiming to enhance value through operational improvements, strategic bolt-ons and financial restructuring," says Hillis.

"There are a number of benefits of selling to a private equity firm, especially if you want to remain involved in your business, scale at speed and have a wealth of experience behind you" adds Ilie.

Impact on valuation: PE buyers are likely to value your company based on its growth potential and the possibility of implementing operational improvements.

3. **A famiy office – a private investment firm that manages a family's wealth – offers a more flexible investment horizon than financial buyers.**

Family offices are a growing source of direct investment in private markets. "They are often more concerned with preserving capital rather than seeking the highest returns, and typically they don't take control of management and operations," says Ilie. "Family offices are looking for businesses that deliver steady returns, paying out income annually and that have a proven track record," agrees Mullin.

"This group of investors only answers to themselves, giving them a simpler decision-making structure and greater flexibility on transaction structure and timescales," says Purvi Amin, Head of UHNW Solutions, HSBC UK.

Impact on valuation: Family offices tend to be passive investors compared to trade or strategic buyers and will offer valuations based on the ability of a company to deliver steady returns over time. They can offer owners greater business stability and more flexible terms.

4. **IPOs, which involve selling company shares on the stock exchange, offer prestige and credibility but also a potential loss of control.**

"This gives businesses an opportunity to raise funds for expansion, enhance company visibility, improve liquidity for shareholders, and increase valuation through market dynamics," says Hillis. "However, it also involves regulatory scrutiny, ongoing public reporting requirements and potential loss of control, making it suitable for businesses ready for these challenges," he adds.

Impact on valuation: IPOs can offer the highest valuation due to market dynamics and investor demand, but can also involve significant costs and regulatory scrutiny.

Getting the most out of a potential sale

While there are many different things to consider with each buyer type, there are simple steps you can take to ensure you get maximum value out of a sale and negotiate favourable terms.

1. **It is important to begin your preparation for a sale early.** "Focus on building a strong financial track record, enhancing business operations, and addressing any potential issues that could affect the valuation," suggests Hillis.

2. **Engage professional advisors as part of your planning and during the sale process.** "M&A consultants, accountants and lawyers can guide you through the process," explains Hillis. "A corporate finance advisor would always be happy to have an informal discussion," says Tillson.

3. **Understand your motivations for the sale.** "Outline your objectives. Be really clear going into that process. What is it that you want to achieve?" asks Amin.

There are many different buyer types that may approach you during your sale, and each will have their own benefits and drawbacks. However, by understanding the Buyer Universe, familiarising yourself with market dynamics, assessing what you want for your business going forward, and preparing early for a sale, you will be well-placed to get the right match for your business exit objectives.

While it's clear that you can't forecast momentous events, what you can do is plan for and prepare your exit strategy, maintaining a degree of resilience throughout.