STRATEGIC BUYER vs. FINANCIAL BUYER: WHAT IS THE DIFFERENCE?

A BUSINESS ACQUISITION & MERGER ASSOCIATES WHITE PAPER

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Determining the best buyer for your business can be a challenging task. Who is the best candidate to take your company and achieve significant success in the future?

Let's look at the differences between two types of buyers vying for good companies: strategic and financial buyers. How might they view and value your business opportunity?

Strategic Buyer

The primary benefit of a strategic buyer is their understanding of your industry. They typically come from a similar or related line of business, or desire a compatible product line to meet the needs of their current customer. This buyer acquires competitors or synergistic companies to achieve the following benefits:

1) ***Grow their size.***
The bigger a business grows the more valuable it becomes. Larger EBITDA generating firms command higher EBITDA multiples when they are eventually sold, compared to smaller companies. Increasing the overall multiple of their combined entity is often the most advantageous benefit to the strategic buyer.

2) ***Adding "strategic" capability.***
Growing customer base, expanded capabilities or "buying versus building" product offerings are benefits desired by strategic buyers. Other strategic benefits include expanding footprint, increasing supplier buying power or better pricing by getting rid of a competitor in a market.

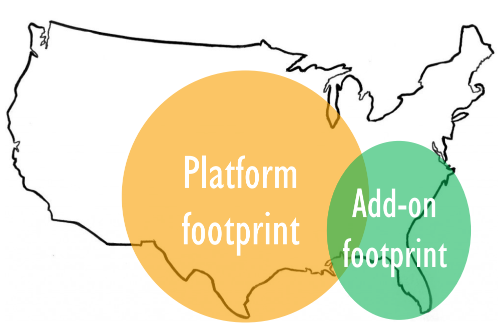
If you can add a strong "strategic benefit" you will likely command a stronger value upfront.

3) ***Gaining tangible & intangible benefits.***
Lastly, strategic buyers often provide attractive offers for complementary companies based on what they can do with those companies after the purchase.

If the strategic buyer has excellent supplier pricing, they can acquire a competitor and apply their pricing against the competitors higher rates generating higher gross margins. Additionally, G&A items like marketing, accounting, taxes, travel, HR management, occupancy costs, shipping, advertising and sales can be centralized allowing the combined entities to run at a lower cost structure than each company individually.

As the seller to the strategic, you'll want to try to capture some value for this increased cash-flow. Strategic buyers often take a stingy position towards sharing in the upside of their savings; however, a good M&A advisor frames a win-win scenario so you can share in some of those savings and benefits to the buyer from the transaction.

Strategic buyers love to expand their footprint and capabilities through strategic acquisitions.



Other items

Since a strategic doesn't have to spend time getting comfortable with the industry due to their strong understanding of the market, they can often close faster and use existing financial relationships to create attractive capital structures for the combined company. Lenders are likely more amenable to providing attractive capital terms for add-on acquisitions from strong performing strategic buyers than to a new financial buyer.

Financial Buyer

If you don't like your competitors, feel strongly about all your employees retaining their jobs after a transaction or desire to keep a stake in your company post-sale, a financial partner/ buyer is likely a better fit.

> If you desire a retained equity stake post-transaction, a financial buyer is often the best option to accomplish this goal.

Financial buyers come in many shapes and sizes and include high net-worth entrepreneurs, corporate buyers and professional money groups like private equity groups, venture capital (VC) firms and mezzanine funds.

These buyers make investments in solid companies with good management teams with the goal of exiting at a much higher value by bringing both capital and some strategic benefits to the company.

Financial buyers generally allow for more equity retention by owners and management. Since many financial buyer groups do not take an active day-to-day role in the company, they look for a strong team who will remain post-closing.

Benefits of financial buyers include the following:

1) ***Less change after closing.***
   Many times, financial buyers look to your management team to remain leaders of the company and drive initiatives. There isn't a big disruption in the chain of command, a facility move or reduction of duplication of costs because the Company is operating as a platform and not being overlaid into a larger parent company.

2) ***Excellent M&A transaction capability.***
   Getting a deal papered and closed with a win-win scenario for the seller and management is old-hat to these deal-making pros. They can structure a transaction and work through diligence with confidence because they are "professional buyers" and they do this a lot.

3) ***Ability to retain equity going forward.***
   Providing meaningful retained equity stakes and attractive equity appreciation capital structures are often part of a financial buyer's toolbox. They can customize an attractive cash-out situation for the seller while also providing significant upside from a retained equity stake in the company.

Financial buyers require your company meet key criteria so they can get financing to provide appropriate returns for equity holders. These criteria typically include the following:

- High recurring revenues
- Low/no customer concentration
- Strong management in place
- Robust market growth opportunities
- 15% or greater EBITDA margins
- Low CAPEX (capital expenditures)
- Fair multiples of EBITDA after CAPEX
- A defendable competitive advantage or niche in the market

Every buyer, whether strategic or financial, tenders a unique perspective to the business transaction and should be considered. A good advisory team will help a business owner review the merits and challenges of selling to both strategic and financial buyers.

Each seller's goals are unique so outlining the best type of buyer for your situation early in the engagement process can add significant value to all parties in the transaction.

Once you outline your goals, stick to them as you plan your exit strategy and review offer letters. If you feel very strongly about your management team remaining in place post-closing but then get a higher offer for from a competitor who will get rid of your entire team, stick to your strategy and find the offer that meets your needs.

Remember that the best offer isn't always the **best price** but rather the **best buyer's best price**. Find the fit first and then negotiate from there.

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