Why Thorough Preparation is Key to a Successful Deal

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With growth in today's M&A market trending steadily upwards and business owner confidence at an all-time high—86% of advisors report owner confidence to be either as good or higher than a year ago, according to a recent industry report by the IBBA—all sectors are expecting an uptick in new M&A engagements. In such a bullish market, the demands on the advisor become more exhaustive. Advisors must prepare materials carefully and sift through low quality listings and potential investors should they hope to close deals.

Evidence of the need for thorough preparedness is already presenting itself in the market; in the first quarter of 2018, the same report by the IBBA showed that nearly half (49%) of deals terminated without closing. Over a third (36%) of deal failures were directly attributable to lack of preparation, from reasons like deal financing falling apart, poor preparation of seller books, lack of negotiation leverage, too few offers, and unrealistic expectations on the part of the seller. Higher deal activity also means there's an opportunity for irresponsible brokers to try to exploit the healthy market.

As M&A advisors, it is our role to foster the best investor-seller match by way of ensuring only quality businesses are signed. Thorough preparation is absolutely necessary in order to accomplish this end goal.

Due Diligence

Before agreeing to represent a seller, an M&A advisor must have a granular understanding of the financial and operational health of the business. This is the only way to match the seller with an appropriate buyer, and is the best safeguard against speedbumps in the negotiation and closing process. As every advisor can attest, surprises in any aspect of the business to the buyer or advisor as the deal is closing is a surefire way to slow down or kill the deal. When performing due diligence of any business, it's key to look at six primary areas:

1. **Traffic:** Traffic is the lifeblood of every post-revenue business. It is vital to have an accurate and verifiable picture of where a business' traffic comes from. The type of traffic, as well as source, will differ from business-to-business. For instance, brick and mortar businesses (e.g., retail stores) are often reliant on various channels of footfall traffic, so it is important to have a clear understanding of these sources and how they stack up to the comps. The sources of traffic will have a significant impact on the business' risk profile if a large percentage of revenue is derived from one source alone, or subject to heavy seasonality. Traffic factors are influential in determining the business' ability to drive leads, its customer acquisition costs, and ultimately, to forecast sales.
2. **Financials:** In any potential acquisition, a complete and accurate picture of a company's future, current, and historical financial position is essential. A well-managed business will have detailed and accurate financial records available from inception. Understanding the unique cost structure of each business is vital to derive its sustainability, especially as cost structures differ greatly between different types of businesses. For example, a retail store will have a much different COGS and OpEx structure used for valuations as compared to an e-commerce store, whose cost structure will have to account for fewer overheads, staff, and likely fewer inventory requirements (more on valuing an online business here). In addition to determining the health of the business, suitors will look to financials to identify trends in growth. Unless there is a strategic angle dwarfing the importance of the financials and overall business health, investors will rarely be ready to execute on an acquisition where the business has an unclear or incomplete financial background. This is especially important where third party financing approval is required.
3. **Buyer and Seller Verification:** Connecting the right investor with the right seller is perhaps the most crucial function of an M&A advisor. This requires an in-depth understanding of the goals of both parties, and begins with verifying that both are representing themselves and their interests accurately and legitimately. By vetting both buyers and sellers thoroughly prior to entering negotiations, an advisor can mitigate the risk of a deal falling through and wasting time and money on both sides.
4. **Operational Verification:** It is imperative to have a clear understanding of the operational requirements for which the seller is currently responsible. A proactive advisor will identify areas where process automation and outsourcing might reduce the need for owner involvement and therefore increase the types of buyers willing to look at the business. This may also fall under exit planning, which can last years but ultimately lead to higher acquisition prices and better terms for the seller. Professional advisors will always win more deals where their reputation is that of someone who puts the exit goals of the owner before their own. By taking the time to go through an exit planning process, an advisor will also gain an intimate knowledge of the business' functions and growth opportunities, which can be a huge benefit when negotiating with potential acquirers.

A Holistic Understanding of The Business

Beyond carrying out thorough due diligence, one factor that distinguishes effective M&A advisors is their ability to form a complete picture of the value and areas for improvement of each individual asset. This requires identifying each business' unique levers of strengths that can be pulled to accomplish different goals by different investors. For instance, a business' financial history may be lacking due to limited investment in marketing and growing the business, but this may not be important to a strategic investor who is interested in leveraging the product in a new way, perhaps by adding it to a portfolio of existing assets. To match the right buyer with the right seller requires the ability to communicate the sometimes-unquantifiable value of the business. Without proper research and preparation, understanding the business' unique selling proposition (or USP) is next to impossible.

Legal Considerations

Understanding the legal complexities involved in both the business itself and deal making means fewer surprises, mistakes, and missed opportunities. Awareness of potential legal pitfalls and the ability to identify and avoid them can be crucial in assessing whether a business is a viable acquisition target. An advisor's legal knowledge and experience will also be invaluable to both buyer and seller in the negotiation and deal structuring stages of any deal.

Honest and Transparent Marketing

Once due diligence on behalf of the M&A advisor is complete, and it is determined that the business is of a sufficiently high standard to go to market, it falls to the advisor to effectively promote the opportunity in an honest and transparent manner. The goal here is not to give the hard sell, but to educate suitable buyers about the business and its potential upside. Preparation of a thorough prospectus (or CIM) is key to effectively marketing the business and reaching the right potential buyers. This should elicit multiple offers, and help ensure achieve the best acquisition price and terms for the seller.

Final Thoughts

Connecting the right investor with the right seller is no easy task, which is a fundamental reason why both parties rely so heavily on the expertise and experience of M&A advisors. Not only does thorough preparedness help identify and navigate any roadblocks on the way to a successful sale, but it is the responsibility of the professional M&A advisor to provide accurate, thorough, and successful service by way of proper research and preparation in a market with more than a few disreputable brokers. By performing fastidious due diligence before marketing the business with candor and integrity, an advisor may well establish a relationship with the seller that extends beyond the initial transaction to result in further deals and brand equity in future.