The Art of the Deal

Insights into the M&A process

By Elise Hacking Carr

The recession may have officially ended in June 2009, but its memories endure. For Jim Anderson, president of Corporate Development Associates, a private intermediary firm located in Scottsdale, Ariz., the 2007-to-2008 era was a "disaster" for mergers and acquisitions (M&A) activity. During that time, industry revenues softened, forcing many printers to merge with other businesses or to close their doors for good.

Current data, fortunately, tells a different story. Thanks to a flurry of deals in the fourth quarter, the 2016 annual total for global M&As finished at a whopping $3.6 trillion, making it the second-best year for dealmakers since the financial crisis, Financial Times reported.

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So far, that momentum has carried over into the print and promotional industry. "This year, we are seeing the most activity than we have over the past several years, both on the buying side and selling side," said Casey Campbell, president and CEO of PathQuest Group Inc., a Fayetteville, Georgia-based private consulting and intermediary firm serving the print and print distribution industries.

Campbell, a 35-year industry veteran who previously worked as president for three prominent manufacturers, including CFC Print Solutions, Printegra and Teraco, focuses on family businesses, privately held partnerships and public companies. Over the past four years, his company has successfully closed 15 transactions ranging from $500,000 to $10 million in value.

"The economy does directly, and indirectly, impact the M&A landscape," Campbell noted. "It's always advantageous to sell your business with key metrics trending to the upside, and we all know that soft economic conditions can negatively impact consumer demand for print and promotional products."

But perhaps the biggest driver of deals going to market, especially in the family-owned sector, is age. "Things are [more] 'robust' today due mainly to an aging ownership, particularly within the printing industry," Anderson said. "Most owners are now in their early '60s or '70s and want to cash out."

This is why it's important to put a well-documented exit strategy in place. "And, the older one gets, the more important it is—every company will change hands at some point," said Anderson, who is celebrating his 30th anniversary as a M&A intermediary. "Some will do it well, and some will not. By the time you are 60, you should begin thinking about who you want to own your company, and perhaps sell no later than age 70."

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Campbell agreed, and added that an exit strategy is more than just timing. "The best exit strategy includes timing related to personal goals, as well as achieving pre-established performance objectives like revenue, gross margins, operating expense, EBITDA and debt-reduction targets," he explained. "Do not forget that your balance sheet needs to be as clean as possible. Most deals we see are asset purchases, and lingering liabilities will impact what you walk away with."

If you're a printer or a promotional products company that's serious about buying or selling, there's much to learn. The good news is, you don't have to go at it alone. Read on as Anderson and Campbell, along with Greg Muzzillo, founder of Cleveland-based Proforma, share their best advice for those trying to enter the deal-making environment.

ON BUYER/SELLER MOTIVATION

The reasoning behind buying and selling is often starkly different. "The decision to buy is almost always to fuel growth to the company's revenues and margins of its core business," Campbell shared. "Sometimes, the decision to buy is to eliminate a competitor from its market, and often it is to provide diversification of its product mix—that is, a print-only distributor buys a promotional products distributor for its expertise to start cross-selling print and promo to its respective accounts."

It gets a little more complicated on the selling side. As mentioned above, age is the primary motivator. But Muzzillo cited additional reasons, including "diminishing sales or personal issues, like the owner's health or a divorce."

ON CULTURAL ALIGNMENT

With any acquisition—no matter which side your business is on—all parties should share a similar vision. "The most successful deals happen when the buyer and seller create a strong relationship," Muzzillo affirmed. "These relationships built on trust, with the common goal of maximizing the success of future sales of the acquired company, make for the most positive outcomes.

"Typically, most sellers and buyers are not on the same page at the beginning," he continued. "... The key, in addition to a strong relationship, is patience. It could take months or years for both parties to finally agree to a deal."

For this reason, intermediaries, especially, can be helpful. "I try to gauge the culture of the seller and prospective acquirers before I even approach them," Anderson said. "Personalities must be in concert during negotiations even if the seller is not remaining with the new owner."

Campbell, who was involved as both a buyer and a seller in more than 15 M&A transactions before stepping into his current role, personally understands the need for alignment.

"Regardless [of whether] we are representing the buyer or the seller, PathQuest follows a specific process that ensures that the business being acquired is represented in the best possible light to ensure a good fit: culture, business processes, go-to-market strategies, product mix, pricing strategies, key vendors, compensation plans, benefit plans, etc.," he said.

In some cases, intermediaries are challenged with representing a pair of sellers who may not be on the same page. Campbell pointed to three common reservations they have:

- A dramatic change in culture
- Negative impacts to employees or vendors post-transaction
- Hesitation about reporting to a new superior, should one of the sellers decide to stay on-board

Anderson prefers to deal with one-owner companies. He offered a cautionary tale about a family-run business to support his logic. "Probably the worst story I have on this topic was with two brothers—their father had started the company and died," Anderson recalled. "One brother was 10 years older than the other and wanted out. At the closing table, with a public company as the buyer, the younger brother offered the older brother the exact same deal, and he eventually took it to preserve peace in the family."

ON POTENTIAL PITFALLS

When asked about the biggest mistake companies make in the M&A process, our experts unanimously answered: unrealistic valuation. "It's easy to understand how that happens," Muzzillo said. "This business is something that [owners] may have poured much of their time, blood, sweat and tears into. Unfortunately, there's no value for time, blood, sweat and tears. ... I have a saying, 'Time makes sellers realistic.'"

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QUICK TIPS

Which factors lead to the most successful deals? Casey Campbell, president and CEO of PathQuest Group Inc., Fayetteville, Ga., offered the following response:

- Being able to demonstrate positive revenue growth in good years and bad.
- Performing consistently at or above your industry's average gross margins, and being predictable.
- Being able to transition leadership to either an internal leader or to someone identified by the buyer.
- Having clean financials. It is OK to have "owner's perks" in your financial statements, but you must be able to identify them, and all buyers will allow you to add these non-recurring expenses back to earnings.
- Being able to manage the due diligence process and continuing to run the business.

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– JIM ANDERSON, PRESIDENT, CORPORATE DEVELOPMENT ASSOCIATES

A number of factors influence accurate valuation, but knowing what buyers are willing to pay tops the list. "In simple terms, nine times out of 10, the buyer's first offer is not enough," Campbell remarked. "While there are multiple ways to calculate valuation, ultimately the buyer determines what [he or she] is willing to pay, and the seller accepts it or not. Here is where competition from buyers favors the seller. Meanwhile, lots of negotiations are taking place. Manufacturing businesses tend to be valued as a multiple of EBITDA, while distribution businesses can be valued on a combination of things like revenue, gross margin and net operating income."

Rejecting outside help is another mistake that happens all too often. "Surround yourself with good professionals—a CPA, attorney, intermediary, etc.," said Anderson, who recently welcomed print industry veteran and Emerging Solutions Now LLC President Roger Buck as an associate to CDA's deal-making team.

ON DEAL STRUCTURES

Finally, there's the issue of deal structures, which is typically presented by the buyer. In order for buyers and sellers to get the structure that is right for them, they must educate themselves on their options. According to Campbell, the two most common types of deal structures are cash purchases and earn outs.

"Sellers prefer a cash purchase for obvious reasons, and buyers prefer an earn out, as it tends to mitigate risks of losing accounts, losing sales/operational talent or a substantial downturn in business," he said. "Cash buyers in this industry are typically a limited number of public companies or private equity firms. PathQuest has been involved in both types of deal structures and is pleased to say that in all transactions, the seller has always received the agreed-upon transaction value. That is not always the case in an earn-out scenario."