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MobileSolve Group, Inc. is a boutique investment bank providing M&A, Capital Raising and Financial Advisory services to technology emerging and growth companies.* This newsletter presents short articles on industry or transaction topics of current interest, and a summary of recent notable transactions.

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WHO WILL BUY YOUR COMPANY?

Among the first items discussed with sell-side M&A clients when thinking through potential buyers for the company is what types of companies should be approached. Most everyone knows there are two main groups of buyers – strategic and financial – but there is less understanding of the several different types of strategic and financial buyers there are, and how they differ in approaching M&A.

Strategic vs. Financial Buyers

Strategic buyers are generally operating companies, probably already active in the seller's sector or a related one. Often the seller has a pre-existing relationship with a strategic buyer, or they are his customer, supplier or competitor, and already know him.

Companies become buyers for many reasons. They may include finding new sources of growth, diversifying the revenue base, procuring customers, expertise or IP, etc. Their valuation approach is to estimate the synergies or economic benefits they would get from the acquisition, and to pay out a portion of those benefits to the seller.

Financial buyers are often funds staffed by consulting and banking professionals that make investments in companies to earn a return on those investments when they exit. They may be less focused on a particular sector, and seek companies with good growth potential supported by sustainable competitive advantage.

Their valuation approach, unsurprisingly, is financial; which often is calculated as an IRR or NPV that can be earned in a sale or an IPO. Aside from a financial buyer that already owns an operating company and is evaluating an add-on investment, there are no estimates of synergies and economic benefits to existing operations found in the analyses of strategic buyers.

Preparing for Different Types of Buyers

Because each type does a different analysis, preparing for a transaction with strategic and financial buyers is different.

Business Evaluation

While both buyer groups will carefully evaluate your business, strategic buyers focus heavily on the financial impact of potential synergies and the risks of integration, while financial buyers look at cash-generating capability and the capacity for earnings growth. Strategic buyers evaluate acquisitions largely in the context of how the company will merge with their existing business.

Conversely, because financial buyers will not integrate the business into a larger company, they generally evaluate an acquisition target as a stand-alone entity which may later be supplemented by other smaller acquisitions. Their focus will be to understand how to increase the long-term value of the company to ensure an acceptable return over their investment horizon.

Integration Analysis

Because strategic buyers will integrate the business with theirs, they will look especially to General and Administrative expenses for cost savings. Back-office functions such as IT, HR, Accounting, Legal, etc., will often be significantly reduced and rolled into their counterparts at the buyer during the post-transaction integration phase.

For financial buyers, the opposite is true. While it is important to demonstrate these functions are managed cost-efficiently, during the due diligence process they will want to see strong departments that can support future growth and possibly integrate add-on acquisitions.

Information Sought

Different strategic buyers will emphasize different things, depending on the rationale of the acquisition. Certainly descriptions of customers, suppliers, technology or R&D and financial performance will be important. Because a strategic buyer may be a present or future competitor, it is all right to provide this information in an oblique way, saving actual disclosure for a single buyer that has made an acceptable offer and provided an executed Letter of Intent.

Financial buyers want to know whether they will be able to sell your company in 5-7 years at a sufficiently higher value than the acquisition price such that the earn their desired return or better. Thus they are interested in examining financial items such as past financial performance, capital structure, and projections, and strategic items such as sources of competitive advantage and potential exits.

Transaction Expertise

Strategic buyers vary greatly in their ability to execute transactions. Many have a corporate development team consisting of individuals with transaction experience. While corporate development will be efficient, approval processes at the buyer itself are likely to slow the pace as management and the Board become involved. It is important to understand the processes of a potential buyer, and where possible to assist it each step of the way.

Such an effort is not necessary for financial buyers, who generally expertly execute deals. Thus they are usually quicker than strategic buyers in closing.

Holding Period

Whether kept separate or fully integrated, strategic buyers assume they will own an acquired business indefinitely. Financial buyers, with their shorter time horizon, think carefully about the timing of their entry and exit. They will want to avoid acquiring a business near the peak of the business cycle only to sell it later at a lower earnings multiple near the cycle's nadir. Demonstrating how the business performs through the business cycle may be important.

Specific Types of Buyers

Moving beyond the generalities of strategic and financial buyers, a seller should consider specific types of strategic and financial buyers, and their advantages and disadvantages.

Companies

The primary advantage of selling to a company is the likelihood it will be willing to pay more than other types of buyers. Thus they are most appropriate for owners who want to exit.

The higher valuation is driven by the synergies attainable in integrating the acquisition. Substantial synergies found in cross-selling opportunities, cost reductions, product bundling, and elsewhere mean higher profitability if executed well.

The sale process should focus on helping potential strategic buyers identify and quantify these opportunities. Of course, cost reductions may come at the expense of employees, and efforts should be made to find those at risk new jobs at the buyer or ensure their smooth exit with appropriate severance packages.

Private Equity

Private equity firms are investment vehicles that manage portfolio companies over 5-7 years, then attempt to sell them for a substantial profit. They thus combine elements of both strategic and financial buyers, though their decisions are clearly driven by financial analyses.

They typically follow one or a combination of several models, such as purchasing a "platform company" as the main operating vehicle in an industry, which in later years is enhanced by add-on acquisitions, or acquiring a control stake in a company with a minority retained by the founders who continue to operate the company with the support of the PE firm. They are most appropriate for sellers who want to retain an interest in the company while gaining the substantial financial and operating resources of a PE firm.

Shell Companies

As meant here, shell companies are holding companies that own a variety of operating companies in several industries. They create value through astute investment decisions and financial engineering.

Like PE firms, they seek a controlling stake in their businesses, but are usually less involved in managing them other than at the Board level. A sale to a shell company may be attractive for a seller that wants to liquidate and diversify most of his equity, but maintain operational control of the company.

Search Funds

Search funds are groups of investors who want to back a particular entrepreneur and buy the company for her to run. The entrepreneur tends to be a highly promising younger executive willing to be guided by the investors.

Search funds tend to operate among companies in the lower middle market or smaller. They are potentially attractive buyers for sellers whose companies are too small for PE firms.

Family Offices

Family offices are essentially private equity firms that are an investment vehicle for a single affluent family rather that a group of institutional investors. They often focus on the industry that earned the family its wealth. They are a relatively new phenomenon born of the increased concentration in wealth at the top of the pyramid.

Because their primary goals are preserving and growing the family's wealth over generations, they tend to be more conservative and to assume longer time horizons than PE firms. This means their valuations may be less than more aggressive investors, but they may also be a more attractive alternative for a founder that wants to stay in the business without the sometimes more intense pressure of PE firms to perform.

Selecting Potential Buyers

While it is important to understand the different types of buyers and their approaches during a sale process, it is equally important not to pre-judge which types to contact and which to avoid. Instead, a buyer list should include potential buyers from several of the available categories to get a diversity of views.

This will result in a wider range of valuations and terms enhancing the options from which a seller may choose. A variety of options will permit a seller to make the optimal choice for life after the sale.

Note: This newsletter if for informational purposes only, and not for the purpose of providing legal, financial or other advice.

Transactions

The following are notable M&A Transactions and Capital Financings announced or completed in the last month.

Notable M&A Transactions

Google acquires Pixel Phone Division from HTC for $1.1 billion. See details here …

Intermedia acquires Anymeeting, a SaaS-based platform providing web conferencing and webinar services for online meetings and webinars. See details here …

LiveXLive Media announced it will acquire SNAP Interactive, a leading provider of live video social networking and interactive dating applications. See details here …

Pacific Office Automation acquires Trans-West Network, a voice over IP and data solutions provider in Phoenix, Ariz. See details here …

Superloop acquires NuSkope, a South Australian-based company which provides fixed wireless services to the home for $10 million. See details here ...

TDS announced it will acquire K2 Communications, a voice, video and data services provider. See details here ...

Notable Capital Financings

Activehours, a mobile app that gives people access to their pay directly from their smartphones, has raised $ 39 Million. The round was led by Andreessen Horowitz. See details here ...

Apica, a Stockholm, Sweden-based company, which provides load testing and web performance monitoring tools for optimizing the performance of cloud and mobile applications, has raised $12M. The round was led by Oxx. See details here ...

Bossa Studios, a London game studio, has raised $10 Million in Series A. The round was led by Atomico. See details here ...

Chime, a leading branchless bank account for the mobile generation, has raised $ 18 million in Series B. The rund was led by Cathay Innovation. See details here ...

iZettle, a mobile payments company, has raised $ 36 million. See details here ...

Lesara, a German online fashion retailer has raised €30 million Series C round. See details here ...

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