TRENDING TOPICS

RETIRING "BOOMERS" MAY BE RUNNING OUT OF TIME

TO MONETIZE THEIR BUSINESS

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At the moment, private equity firms are bursting with capital, and strategic corporate buyers have access to funding at historically low rates. It's a sellers' market for middle-market companies at an opportune time for those baby boomer owners who are ready to retire.

But will it last?

If you have decided to monetize your business, you might be well advised to move fast. While it takes time to position your company for an advantageous acquisition, M&A markets can be quickly snuffed out by unanticipated events, such as a housing bust. And the wave of baby boomer retirements has been going strong for 10 years, meaning competition for deals will only accelerate as more and more boomer-owned companies enter the pipeline.

IMPORTANCE OF PLANNING RIGHT NOW

Owners looking to sell larger middle-market companies with more professional management and operational infrastructure should start considering their options three to five years in advance, advises Michael Hand, managing director at PNC Riverarch Capital, a private equity affiliate of PNC.

Less lead time may be needed for owners selling majority or significant minority stakes in their businesses in order to diversify risk or bring in additional capital and know-how. But those looking to eventually hand over control need to resolve numerous issues before executing a successful sale.

EVALUATING POSSIBLE BUYERS

One task is evaluating the range of potential buyers. For example, your competitors may be able to pay more for your company due to traditionally cheaper cost of funding, although this is less true today given financial firms' abundance of capital to support bids. Potential synergies can also boost competitors' firepower, although that could mean significant layoffs and the elimination of owner-related branding — tough pills to swallow for some owners proud of the companies they built. Ultra-wealthy families sometimes establish family offices to manage their financial affairs.

When buying a company, such family offices are more inclined to retain the corporate and management structures. However, their acquisition process tends to move at a much slower pace and they typically look for companies providing extremely consistent income.

Wealthy individuals and "angel networks" of investors are also potential buyers, but the vast majority of sales today are made to private equity firms.

MANY ISSUES TO TACKLE

If you're an owner/operator, you must groom a stand-alone management team, including a replacement chief executive. A multiyear lead time may also be necessary to resolve lingering issues that could complicate the sale process, ranging from environmental challenges to problematic customer relationships to legal disputes.

Hand notes that business owners often fail to address tax and estate issues. "The three people a business owner should be talking to well in advance of selling the business are his or her attorney, tax advisor and investment banker," he says.

RETAINING "SKIN IN THE GAME"

Owners must also consider the level of involvement they'll want in the company after the sale. Especially for acquisitions at the smaller end, private equity firms will want the owner to retain some "skin in the game," usually in the form of an equity share of 10% or so, or subordinated notes of a few years in maturity with a performance-based payout.

The sale agreement "may have certain provisions, depending on how aggressive the deal is, where the senior lender can cut off interest or principal payments on the note if the company is squeezed a bit," says David Mengel, executive vice president of Business Development at Steel City Capital Funding, a specialty finance company affiliate of PNC.

And rather than extracting significant compensation through dividends or other means, Hand says, owners will probably be offered more market-oriented compensation, such as a salary and a bonus based on the company's performance.

As you evaluate private equity groups relative to a sale, make sure the PEG's financial institution has a reputation for getting the deal done and not flinching as markets gyrate.

YOU MAY NOT HAVE TO SELL AT ALL TO MONETIZE

With new and creative recapitalization finance available to business owners, a little leverage can go a long way. Putting the right combination of junior and senior capital in place through a delicate leveraging of the company can often be a great first step to monetize the business prior to putting the plans for sale into action. Seeking lending relationships with financial institutions with deep experience in these structured capital situations is essential to your success as a business owner.

In a market ripe with opportunities, leveraging a little pro-active planning and the right team of advisors can make your transition from driving your business objectives to riding into the sunset easier and more profitable.

A MARKET ABOUT TO COOL OFF?

The market for middle-market acquisitions remains hot by historical measures, although it's showing signs of cooling. *The Lead Left*, a capital markets newsletter focused on the middle-market space, reports that private equity funding fell somewhat in 2014 from the year before, although it remains well above the levels of the previous four years.

"We're at the point now where the market is close to its peak. That doesn't mean it's going to collapse, but it also suggests there's not much upside," Hand says, adding that, assuming the critical issues around monetizing a business have largely been addressed, "Why wait any longer?"

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