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EXIT STRATEGY: POSITIONING YOUR COMPANY TO BE SOLD OR ACQUIRED

If you were given a 50 percent chance that your company would fail after acquisition, would you take those odds? What about 75 percent – or even 90 percent? While there are a multitude of risks in starting a company and in making one successful, there can be an even greater risk of failure in being acquired.

That's sobering news for innovative entrepreneurs and their startups. But it doesn't have to be that way. Here's how to put yourself on the plus side of those statistics and favorably increase your odds for a successful exit.

Trends in the Marketplace

It's no secret that current trends in the marketplace can have a big impact on whether a company is an attractive contender for acquisition. Peter Longo, executive vice president and chief investment officer for Connecticut Innovations, says many acquisitions are driven by the markets. "When trends are positive, it's good for acquisitions; more money is available. But exits can also happen in not-so-great markets, especially in the pharmaceutical markets. Large companies are always looking for growth opportunities, so there is no shortage of opportunities for acquisitions."

Indeed, with the high cost of entry into many markets and the time it takes to start a new company or division complete with top development talent, companies instead look for acquisitions that can help now rather than later, especially to fill one or more gaps. "Acquiring synergistic and complementary products or solutions can create significant value for the acquirer," notes Eric Rosow, founder and former CEO of Premise Corporation and now chairman of ReadyDock and president of Scry Health. "They look at the opportunity to get into new markets or acquire new customers that the buyer may not have any relationship with. The buyer may not have a presence in a particular market or with certain customers, but that could be improved by acquiring another company's products, people and customers."

To that end, one of the most important rules of the acquisition game is to build a company that someone wants to buy rather than one you want to sell. Often a CEO or management team becomes too preoccupied with selling a company rather than continuing the solid work of making that company the best in its field.
Staying focused on running the business in the normal course will attract buyers. "There is nothing more important than good performance. When companies lose momentum or suddenly have problems in the business, either transactions fail or valuations are reduced," says Gary Mathias, managing director, Carter Morse & Mathias, and CFO and board member of Thetis Pharmaceuticals. Staying

the course and doing the things that have brought you to a profitable and enviable position in the marketplace is a priority.

David Wurzer, senior managing director of investments, Connecticut Innovations, agrees. "It's not about yelling louder. It's about building a company that a buyer will say is doing all the right things, and it would be easier to buy it than build it from the ground up. Buying often eliminates barriers to entry and lowers the risk. That's what buyers are looking for: a better mouse trap."

Looking for a Strategic Fit

Your chance for acquisition success has much to do with strategic fit. It's not just about making the most from your exit strategy, although negotiating a good deal is certainly a top goal. You need also to remember that this is a company that you and your management team have built from the ground up. You've hired great talent, developed innovative products or services, and cultivated an enviable reputation among your peers. A bad fit can ruin both the acquirer and the acquiree and leave customers, and employees, with a sense of betrayal.

Rosow, who sold his healthcare company, Premise Corporation, in 2008, says that strategic fit was one of the most important things to remember while positioning his company for sale. "For me, there was never any doubt that I wanted to sell to the right buyer. When we were

considering buyers, I made sure we looked at fit. Did the buyer have the same vision? Did it see things the same way we did? Did our culture fit with the buyer's culture? Premise had a very open culture where a balance between employees' personal lives and work was important in creating a productive work environment. I wanted to make sure that, for the most part, that would remain intact."

For Premise, the acquisition worked well. It gave the company an international reach that it might not have gotten on its own, and it gave the buyer innovative products highly valued in the industry. Not all mergers or acquisitions are as successful. Consider the disastrous acquisition of AOL by Time Warner. Five years after the merger, Time Warner unloaded AOL, losing billions in value and with nothing to show for the partnership. Poor fits don't survive; more often they implode.

If an acquisition is part of your exit strategy, make your company attractive to potential candidates, but keep your options open. While strategic buyers – those who have a working knowledge of your type of business or those in your industry – may be ideal and could offer you the most lucrative deal if you have the critical capabilities needed by the acquirer, don't rule out private equity buyers. These potential buyers often have deep pockets. Keep in mind that private equity buyers are concerned mostly with EBITDA, or cash flow, and will use debt financing to pay for part of the acquisition cost.

"If someone comes to a CEO and is interested in buying his or her business, the CEO should be receptive to talking. It's never a bad idea for CEOs to talk about their companies," says David Audibert, managing director of investments, Connecticut Innovations. "That's business development and good practice. Listen to a potential exit opportunity, and be open-minded and flexible. But don't give too much information; be protective." Indeed, when it comes time to reveal information, you need to be comfortable with the people you're talking with. You need to vet all interested parties and understand their businesses and motivations.

Beware the Wormhole

While you vet the buyer, the buyer is going to vet you. Being prepared in all ways financially and operationally will put your company in a favorable light. "You want to be bought, not sold," says Longo. "The best premiums are paid when a buyer just has to have your company." If you're not prepared, it will be readily apparent. But don't make matters worse by overselling or overstating your company's position. "You'll find yourself down a wormhole pretty quickly if you're stating or portraying things inaccurately," says Audibert. "Everything comes out during due diligence."

Why risk everything you've built? Not every company is perfect, so if there is a hiccup or two in your performance history, bring it on. As an

investment banker, Mathias has seen a range of weaknesses and strengths in the more than 50 M&A transactions he has handled. He recommends clients get clarity about post-closing integration to avoid critical failures that can impact customers, suppliers and employees. Additionally, he advises seller clients to avoid buyout transactions that overly leverage a company. While leverage can help make a transaction happen, it can preclude taking advantage of growth opportunities in the future and also increase risk of business failure if the company hits a bump. What about these concerns? Mathias says to "find an acquirer that has been there before, who has a strong record of working with management teams to integrate the business and has seen companies through tough times without running for the exit."

What this all boils down to, again, is the critical focus on building your business. You can't lose sight of creating value. An exit strategy is years in the making and not something to take lightly. "Start preparing years ahead, identify the likely strategic buyers and build the company accordingly," says Mathias. "Hire good accountants and lawyers along the way to make sure your house is in order, build strong management teams, make yourself expendable, invest in systems to track key financial and operating metrics, and drive performance based on these metrics."

This good advice will likely keep you from tumbling down the wormhole.

Ask for Directions Along the Way

No one knows everything. Although it's tempting to try to oversee and control every facet of your exit strategy and positioning process, it's much wiser to ask for help. In fact, building relationships with other CEOs or management teams might bring you in contact with future buyers.

Wurzer says that third-party opinions, especially relative to market position, are important. "Setting a strategy that's coming from an independent view is very helpful and removes much of the emotion. Often CEOs can be sensitive about how they stack up to the competition, but an honest appraisal, where an advisor can detail what the company is good at and what the competition might be doing better, is necessary. Get that advice earlier in the game rather than later. It's easier to work an acquisition if it's not a fire sale."

Rosow agrees that there is nothing wrong with having confidence and optimism, but not so much ego that you can't ask for advice. "It really does take a village. I'm not the type of CEO who knows everything. I am constantly reading trade journals and business content and talking with and learning from other CEOs and founders. They, along with board members, are a great source of ideas and points of view."

You've worked hard to build your business and plan a favorable exit. The upside to acquisitions can bring numerous tactical and market advantages to the buyer and huge strategic advantages to you, as the seller. If you understand your business thoroughly and keep your focus on creating value through great management, a sustainable market position and margins, recurring cash flows, and diversified revenues, you'll be better positioned for a successful and profitable exit.

NOTE: Special thanks go to several individuals who were interviewed for this article and whose insights are incorporated herein. They are:

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Eric Rosow, *founder and former CEO of Premise Corporation and now chairman of ReadyDock and president of Scry Health*
David Wurzer, *senior managing director, investments, Connecticut Innovations*

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