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Advice & Planning

Business Transition Planning Spotlight

Private equity group vs. strategic buyer

By: Steve McConley — Wealth Planning Business Transition Strategist, Wealth & Investment Management, Wells Fargo Bank, N.A.

It can be overwhelming to think about selling your business to somebody else. One way to gain some control is to be informed about your alternatives so you better understand what is best for you, your family, and your company. While buyers come in all shapes and sizes, perhaps the most sophisticated buyers are private equity groups (PEGs) and strategic buyers. What are these buyers, and what can a business owner expect from them?

More information:

Private equity group vs. strategic buyer

Next month:

Management buyout vs. employee stock option plan (ESOP)

Upcoming call:

What is an ESOP?

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First, we should start with some definitions for our discussion:

- **Private equity group: a group that raised a pool of money (a fund) in order to buy companies**
- **Strategic buyer: a buyer in the same or related industry that has a synergy that could result in cost savings and/or revenue enhancements**
- **Deal structure: describes what you are selling along with payment terms and timing**
- **Transaction currency: what you get from the buyer (for example, cash, note, buyer stock)**
- **Rollover: when you reinvest proceeds back into the company alongside the buyer**
- **Intended holding period: period the buyer intends to own the company**

Traditional PEGs raise a fund of money to buy companies with the expectation of selling them in a few years and returning the proceeds to investors. Their goal is to earn high returns for their investors. They pay cash and often recommend you roll over (or reinvest) some sale proceeds to own a minority stake as you and your management team continue to run the company. This incentivizes you to optimize company performance in order to enhance the subsequent sale. That subsequent sale can be lucrative, but it is uncertain and you need to consider the longer time horizon to a full exit.

	Private equity group	Strategic buyer
Speed of transaction	Often relatively fast	Varies
Deal pricing	Market price multiple of cash flow	Often highest — each is unique
Deal structure/financial goals	100% sale with reinvestment Selling rollover can be lucrative	Usually a single 100% sale
Company/community legacy	Uncertain as company will be resold later	Company likely to be absorbed, leading to loss of legacy
Employee security	They rely on your team	More risk of job loss for leaders
Your retained risk	Some cash today, some at next transaction — relatively high retained risk	More certainty with a single deal if for cash — relatively low retained risk
Buyer's planned holding period	Typically three to five years	Indefinite

A strategic buyer is an industry participant who usually buys your entire company in a single transaction, paying in cash or company stock. They do not intend to resell your company, but they may be more of a threat to your managers' employment depending on overlaps with their existing management team. Acquisitions may not be their first priority, and each has their own approach to valuation and timing. Often, their culture overwhelms that of the seller, so you will want to understand their long-term plans for your company if your legacy is a priority for you.

No one type of buyer is universally better than another and suitability for any seller is dependent upon their objectives, so it pays to be open-minded and informed. The Business Transition Planning team can help you find your best alternative. Please contact your relationship manager to learn more.

Disclosures

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