

Facilitating Corporate Change- Amalgamation/Acquisition/Sharing

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Topics for Discussion



HAVING A STRATEGY

- Why are we doing this?
- Internal Due Diligence
- What do we actually need?



ASSESSING

- Finding Targets or Partners
- Valuations
- External Due Diligence



NEGOTIATING

- Defining the deal
- Term Sheets
- Contracts



IMPLEMENTING

- Business integration
- Realising value
- Dealing with reality

How much time should I allocate?

1% → 99%

1. Having a Strategy
2. Assessing
3. Negotiating
4. Implementing

Learn from the mistakes of others. You can never live long enough to make them all yourself!



How much time should I allocate?

1. Having a Strategy **40-50%**
2. Assessing **20%**
3. Negotiating **5%**
4. Implementing **25-35%**



What do the academics say...

...acquisitions did not enhance acquiring firm value...

...acquisitions were found to erode acquiring firm value and produce highly volatile market returns...

...target shareholders generally fared well, often experiencing significant positive returns...



Reasons to consider sharing, merging or acquiring...

- Increased efficiency ($1+1 = >2$) *
- Improved performance (I can run it better) *
- Better resource deployment
- Better buying power with suppliers
- Get a better management team
- Value creation through increased market power
- Consolidate to remove excess capacity from market/industry
- Accelerate market access for products through channels
- Customer lists
- Increase brand awareness
- Diversification of products (horizontal) *
- Integration of supplier to increase margins (vertical) *
- Get skills or technologies
- Economies of scale *
- Grab a start-up with potential to be a winner *
- Owner wants to retire/succession planning
- Business looks cheap *
- Self-interest (With more revenue I can increase my salary) *
- Share cost of industry regulation
- Others...

(* BUYER BEWARE!!!)



Reality...

- Almost impossible to realise to the levels initially thought
- Additional costs in the short term can outweigh future gains

Synergies

If the only driver for the deal is realizing synergies – don't do it

Economies of Scale

- Work better if business has low margins to start with
- Better buying power usually comes with higher volume orders:

Warehousing? Working capital?

- Managerial capability

Can my guys manage that size of team?

Having a Strategy...

Internal Due Diligence

- Understanding your own business first -what gaps do you need a second business to fill or where are the best synergies going to come from

1. Market position, market performance and direction
2. Products and Services – Customer fit
3. Internal operational efficiency
4. Financial performance and working capital
5. Culture and organizational structure/performance

Actual Output of
Business Surveys
completed by
Senior
Management of a
Wholesale
Distribution
Business

	1. Market position, market performance and direction						
RISK LEVEL	High	Relatively High	Medium	Relatively Low	Low	1 or 2	Skipped
Cabernet						7	0
Shiraz						2	1
Merlot						2	0
Riesling						5	1
Pinot						5	0
Muscat (Based on Q's answered)						3	9

	2. Products and Services – Customer fit						
RISK LEVEL	High	Relatively High	Medium	Relatively Low	Low	1 or 2	Skipped
Cabernet						3	1
Shiraz						1	0
Merlot						2	0
Riesling						2	1
Pinot						2	0
Muscat (Based on Q's answered)						0	5

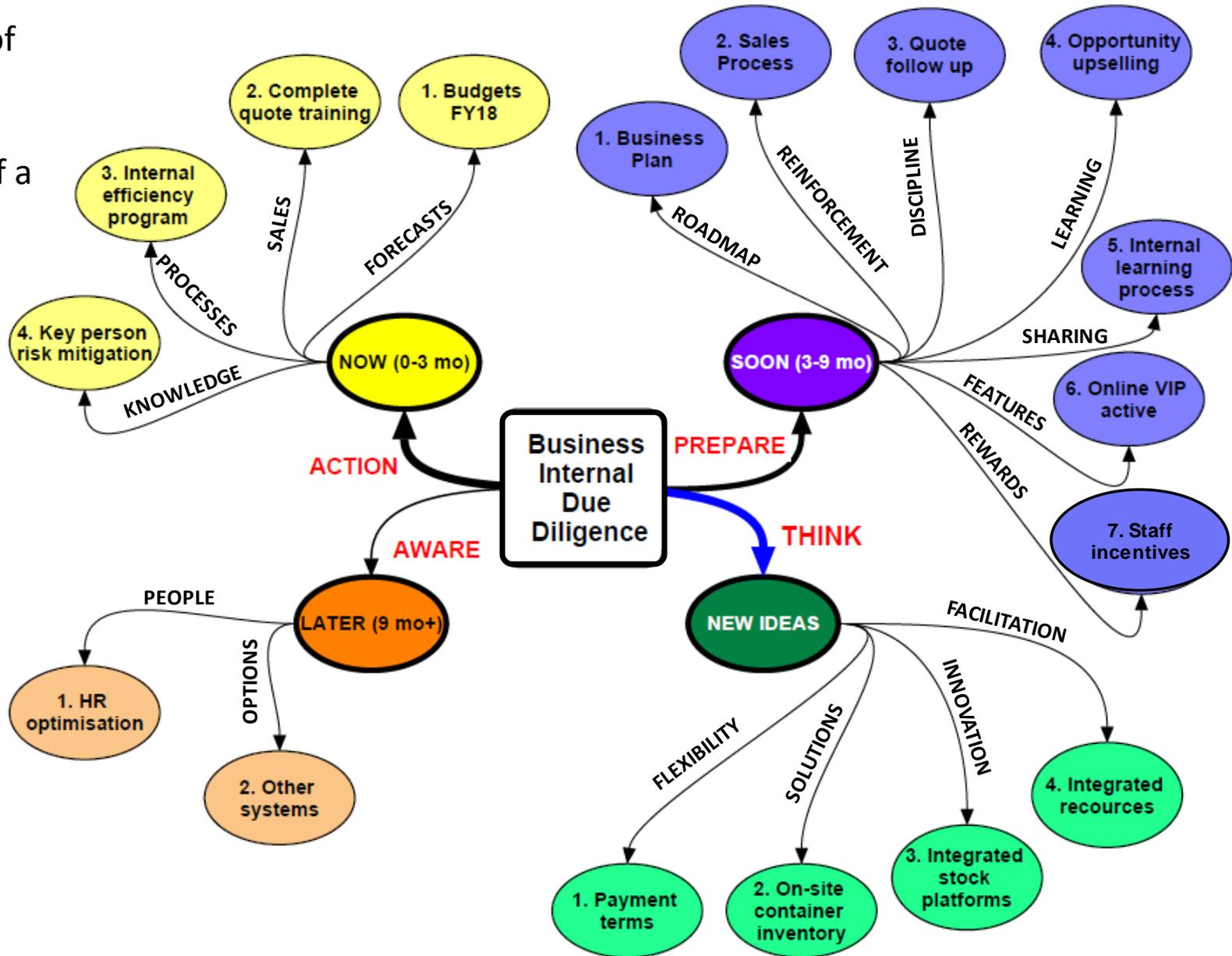
Scores = 1 to 5
1 or 2 indicates
high risk (low
performance)

	3. Internal operational efficiency						
RISK LEVEL	High	Relatively High	Medium	Relatively Low	Low	1 or 2	Skipped
Cabernet						2	0
Shiraz						0	0
Merlot						8	0
Riesling						1	0
Pinot						0	0
Muscat (Based on Q's answered)						1	0

	4. Financial performance and working capital						
RISK LEVEL	High	Relatively High	Medium	Relatively Low	Low	1 or 2	Skipped
Cabernet						2	0
Shiraz						1	0
Merlot						5	0
Riesling						4	1
Pinot						2	0
Muscat (Based on Q's answered)						0	6

	5. Culture and organizational structure /performance						
RISK LEVEL	High	Relatively High	Medium	Relatively Low	Low	1 or 2	Skipped
Cabernet						7	0
Shiraz						0	0
Merlot						6	0
Riesling						4	1
Pinot						3	0
Muscat (Based on Q's answered)						1	3

Actual Output of Workshop with Senior Management of a Wholesale Distribution Business



Assessing...

Where would you look for targets

- Local competitors
- Businesses already known to you
- Knowledge of retiring owners
- Business network contacts
- Business broker sites
- Distressed sale sites (e.g. Resolve)
- Hire someone to look (or sell) for you (*monthly retainer + % on deal price*)



<https://www.resolve.expert/>

Buy and sell private or distressed businesses.

	Kangaroo Tent City & BBQs (Administrators Appointed) Voluntary Administration \$5m - \$10m Turnover p.a.	Jirsch Sutherland 44 Staff Retail Trade	>
	Custom Bus Australia Pty Ltd (Administrators Appointed) Voluntary Administration \$50m+ Turnover p.a.	Worells Solvency and Forensic Accountants 133 Staff Manufacturing	>
	Ocean Health Systems Voluntary Administration \$1m - \$5m Turnover p.a.	BRI Ferrier 15 Staff Software	>

Assessing...

Valuing potential targets

- Get yourself valued... (e.g. Bizdiligence basic repc
- Get familiar with valuation methods
 - Multiple of profit
 - Value of future cash flows
 - Other incl. goodwill
- What would your return be vs putting money elsewhere



Brett Goodyer



BizDiligence Appraisal Report

\$2,499 ex. GST

Knowing what a business is worth is often the first step... Whether your aim is to purchase a business, prepare a business for sale, to reach a commercial settlement to finalise a dispute, or simply to understand your business more thoroughly, we will not only provide those answers, we will explain it in easily understood, jargon free language.

<https://www.bizdiligence.com.au/>

Assessing...

Due Diligence Process

- Financial – with Accountant
 - Legal – with Lawyer
 - OH&S
 - Environmental
 - HR
 - Cultural
 - Business sustainability...
- } with specialist advice



Critical for **share sales** as you are inheriting the liability for past actions

Always try and back up with warranties in contract

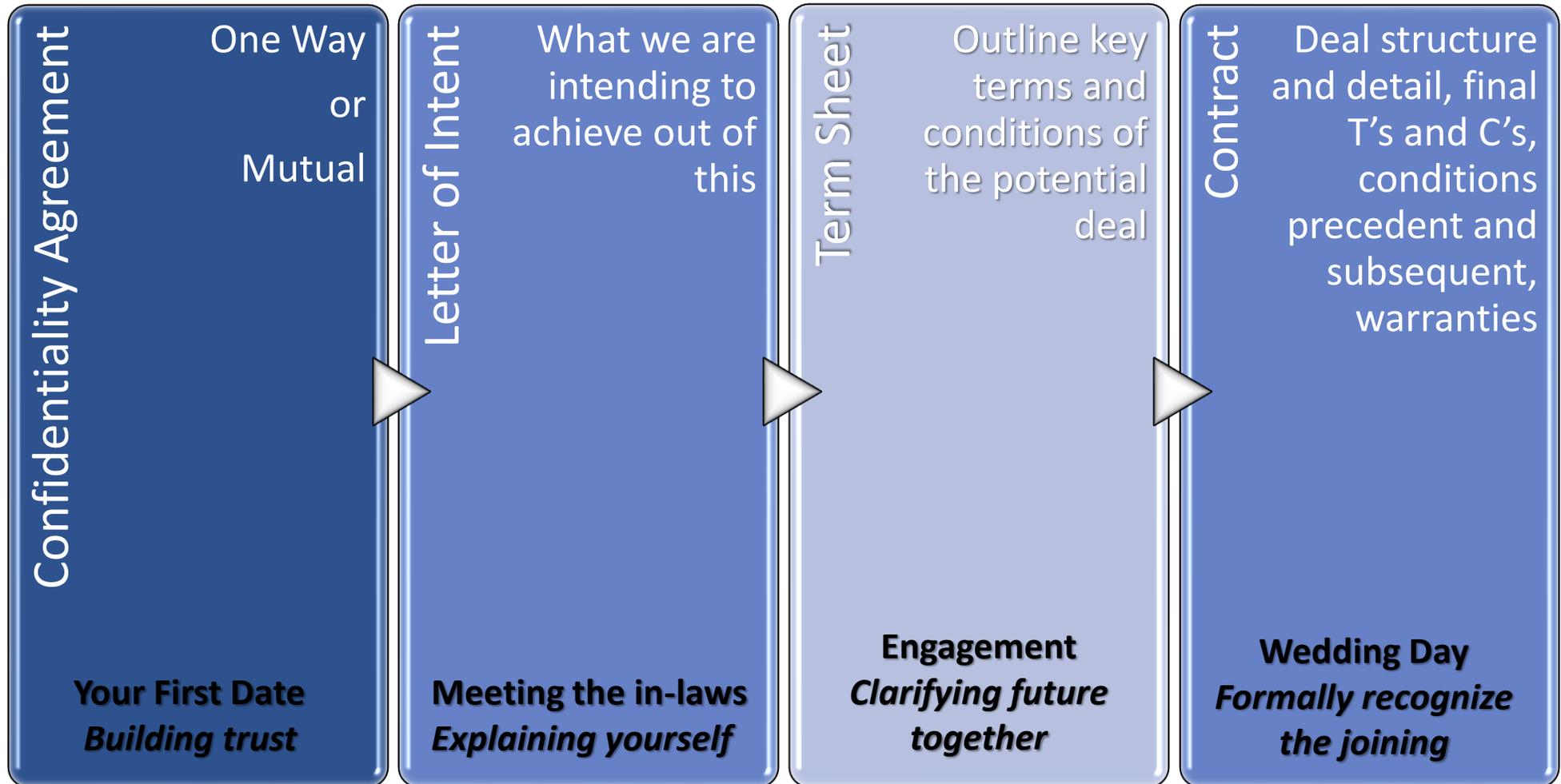
The 'Information Memorandum'

- Usually written by broker if looking at business in formal sale process
- Can write your own with the help of an advisor – plenty of templates for ASX listed entities

Potential contents list

INTRODUCTION	3
FINANCIAL SNAPSHOT	3
OWNERSHIP AND HISTORY	4
NARRATIVE AND DESCRIPTIVE INFORMATION	4
Industry Overview	4
Overview of the Business	4
Ownership and Control	4
History of the Business	4
Strategy and Business Model	4
Customers and Customer Relationships	4
Products and Services	4
Market Segments	4
Competitive Overview	4
Company and Product Brands	4
Sales and Communication	4
Industry Trends	4
Management and Employees	4
Operations and Business Process	4
Facilities and Premises	4
Vendors and Supply Chain	4
Information Systems	4
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Assessing... Protecting yourself and documenting your journey...



Confidentiality Agreement

Non Disclosure Agreement

1 Pager 20 Pager

- Plenty of examples all over the web to download and build yourself
- Key clauses – **one way or mutual**
 - I want to look at yours and won't tell anyone
 - I want to look at yours and you can see some of mine and neither of us will tell anyone
- Timeframe – try for 3 years
- Add in any other conditions you feel necessary
 - E.g. Banned from approaching/poaching staff



Letter of Intent

Different from 'Indication of Interest' = lays out more specific details/terms

- Usually asks for period of 'exclusivity'
- Usually includes an indication of timeframes for further due diligence
- Usually mentions key areas of information still need to review
- Usually defines a desired outcome if successful
- May not include a price, but may include a potential method of valuation
- **Don't lock in anything in here you know you will be disagreeing to later**
 - Not legally binding – but destroys trust in negotiations
 - OK to list options and then pick one later

Term Sheet

The real nuts and bolts of the deal – I usually use a **‘table’** within a letter

#	Term	Explanation
1	Parties	Which company is buying which company (correct legal entities)
2	Shares or Assets	Define what exactly is being included in the transaction
3	Pricing	Method of valuation or agreed price, any ‘earn-out’ clauses, when money will be paid (at settlement or in tranches)
4	Conditions Precedent	What has to be done before settlement can occur (removing personal items from balance sheet, finalizing financial reports)
5	Conditions Subsequent	What has to be done after settlement (usually include a timeframe)(resign as director, sign over domain names, change bank accounts)
6	Key Staff	What key staff will be required to sign retention agreements
7	Other Terms	As many as you like...the more detail the better for clarity between the parties

Get the lawyers to look at it as they will be using this as their basis for drafting the contract later...



Contract

The final legal document –

Check it carefully with your
*lawyers...they can also make mistakes
sometimes*

- **Warranties** – even though you have signed off on Due Diligence – use warranties to ensure that there is nothing you haven't been made aware of!



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Negotiation...

- Prepare your scenarios in advance
 - Know your BATNA*
 - Listen
 - Be rational
 - Be fair
 - Justify your position
 - Appreciate their position
 - Don't haggle for the sake of ego
- *Remember the lawyers are on the clock...*



Done badly can destroy a deal



*BATNA = Best Alternative To No Agreement

Negotiating...

Think through the deal options

- Assets or shares
- Price
- Earn-outs (if any, calculation process)
- Stock value
- Key staff retention
- Handover period
- Non-compete restrictions
- Conditions precedent (Clean up tasks)
- Conditions subsequent (Must do later)
- Warranties (Legally promised) and time period
- Payment terms (bank debt, Vendor finance)
- Good leaver/Bad leaver terms if staying on
- Partnership parameters
- Profit sharing and dividend policy
- Board voting rights and new shareholders agreement



Integration...the hardest part!

What should we be looking out for?

What should we have planned in advance?



Integration...the hardest part!

Employees

Who are they letting go to save costs?

The company has more debt now, my bonus will be cancelled

I don't want to move to another location

Who is my manager now – what do they know about my role?

They just care about making money

Do I have to sign this new contract?



I feel terrible, half of my team has been let go

Who will do all the extra work now they have downsized the team?

Integration...the hardest part!

Operations

- Complexity of IT Platforms
- Stock purchasing and control processes
- Warehousing capacity and costs
- Safety and compliance standards
- Order picking paperwork
- Customer invoicing process
- Customer and supplier payment terms
- Management structures and authority
- Warranty and repair conditions
- Wage rates and payroll processing
- KPI's, measures and rewards
- Customer perception of change
- Maintaining service quality
- Internal staff morale
- Communication channels



“IT'S A GREAT ACQUISITION, BUT WE MAY NEED HELP GETTING ALL THESE PARTS TOGETHER CORRECTLY.”

Integration...the hardest part!

Resentment and distrust by acquired staff

Efforts to sabotage operations (former owner, employees)

Talent flight to competitors

Cultural issues

Working capital

- servicing additional debt
- paying redundancies during downsize*
- increasing stock holdings across multiple locations

* Negotiate into price or leave surplus employees with old entity

Benefits of growing through M&A

- Renewed energy in the business
- Getting down to writing a business plan
- Being serious about planning for the future
- Succession planning ability
- Less reliance on few key staff
- Skills and Technology transfer
- Brand refresh
- New message to take to market/customers

Any other Questions?



“ I love your business model!”

Thank You



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