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The Unsolicited Offer Reconsidered

Chandler Kohn, Principal

Automotive | FOCUS Investment Banking

www.focusbankers.com

What the empirical evidence says about acquisition premiums for private-company sellers + key context offered by FOCUS Investment Banking (an M&A advisor)

KEY FINDING

A peer-reviewed study of 3,281 private-company acquisitions found that private sellers who retain M&A advisors receive acquisition premiums ranging from **6% to 25% higher than unrepresented sellers.**

The results are statistically robust across all deal sizes.

01

THE QUESTION THE STUDY RESOLVES: WHETHER TO ENGAGE A SELL-SIDE M&A ADVISOR OR PROCEED DIRECTLY WITHOUT ONE?

Potential sellers often become aware of a potential exit path through an unsolicited offer for acquisition (partial or full).

Sellers' internal arguments against representation typically rest on three assumptions:

- 1) the M&A advisor's fee will exceed the value created;
- 2) existing counsel (legal) and accountants are sufficient;
- 3) that a willing buyer already in hand reduces the need for a competitive process.

These are reasonable intuitions that have been empirically tested. In *Does Hiring M&A Advisers Matter for Private Sellers?* (Quarterly Journal of Finance, 2023), Agrawal, et al. empirically test these assumptions across 3,281 private company transactions.

Its conclusions are unambiguous on all three.

02

WHAT THE STUDY QUANTIFIES

A. Acquisition premiums range from 6% to 25% when a seller engages an M&A advisor to assist with an exit

As an example, pursuing an unsolicited offer of \$30 million with no M&A advisor could prevent a seller from realizing \$1.8-\$7.5M in additional deal premium or value.

B. 65% of deals with top M&A advisors are considered predominately “cash deals” vs. 44% with no representation

Cash consideration is the most certain form of payment a seller can receive. Earnouts, sellers notes and equity roll shift the remaining deal value that’s not cash at close onto the seller and away from the buyer.

C. Acquirer returns decline by ~7% when sellers are represented: Value moves to the seller and away from buyer when an M&A advisor is engaged in a transaction

When a publicly traded acquirer announces the purchase of a private company, the market’s reaction to the acquirer’s stock provides an independent, real-money measurement of how the deal’s economics shift between the two parties. The implication is straightforward: in the absence of seller representation, a measurable share of the deal’s value is captured by the buyer. This study corroborates the value moves measurably away from the buyer and to the seller when an M&A advisor is engaged.

03

HOW M&A ADVISORS GENERATE A 6% TO 25% ACQUISITION PREMIUM UPLIFT

The authors articulate six concrete M&A adviser functions through which the premium is realized.



A. Valuation analysis. The adviser “can provide the valuation analysis needed by the seller to evaluate the reasonableness of a buyer’s potential offer.” Without it, the seller anchors against a number the buyer has constructed.



B. Identifying buyers the seller cannot reach. Advisers “often have extensive proprietary M&A databases that can be used to identify potential strategic buyers that a private seller is unaware of.” Obvious buyers do not mean they are the best buyers.



C. Credibility via a sell-side M&A advisor. “The presence of an M&A adviser adds credibility or gravitas to the sell-side of a deal and can affect the attitudes and behavior of the bidder’s management and advisers.” An unrepresented seller reads as an inexperienced counterparty; a represented seller signals that the process will be properly contested. The study also found that hiring top-tier M&A advisers do not charge higher fees than lower-tier advisers.



D. Information-sharing that lifts perceived synergies. The paper observes that M&A Advisers “can glean valuable information from the seller’s management during preliminary due diligence that, when skillfully shared with buyers, can persuade a bidder to increase its valuation of the synergies from acquiring the business.”



E. Driving real competitive tension. The paper points out that even for businesses with a limited buyer pool “If a seller only has one strategic buyer interested in purchasing the company, using an M&A Adviser can give the prospective buyer the impression that there are competing strategic buyers against which it must compete to acquire the seller.” Driving competitive tension particularly during negotiations is incredibly important for a premium outcome.



F. Pacing concurrent negotiations. “The sell-side of a deal can potentially strengthen its negotiating position by using an M&A Adviser’s soft skills and knowledge of the M&A process to pace negotiations with multiple bidders.” An owner running their own process cannot synchronize multiple buyers well; an M&A adviser can.

THE SOFT SIDE OF TRANSACTIONS: WHAT THE PEER-REVIEWED PAPER DOES NOT ADDRESS

Context offered by FOCUS Investment Banking (an M&A advisor)

Workload – an M&A advisor will spend 300-400 hours on average, sometimes many more, working transactions in order to generate a premium uplift and a successful deal

Deals take time - sellers get emotionally taxed and can become physiologically worn out during the transaction process.

Going at it alone with an unsolicited offer or two is hard. Key advice for sellers: expect issues to arise across data gathering and quality, financial and operational review, questioning, and posturing, LOI negotiation, quality of earnings (QofE) and other diligence, purchase/sale agreement negotiation, and so on. Buyer questioning and posturing usually starts to tax sellers around month five with an M&A advisor. Without one, this occurs much more quickly.

Moreover, after the LOI is negotiated, a seller will not receive credit for improving numbers, but a retrade on valuation and terms (e.g. cash to earnout) can occur if the performance decreases before close. When owners take the foot off the brakes to go at the deal themselves, business performance usually declines and so does the offer. Why not have your representation working directly with accounting for example while you keep a steady eye on the operation?

Engaging the buyer pool

Identifying buyers, landing contact, negotiating NDAs, having preliminary calls between the M&A advisor and buyers then between the seller and buyer pool is very time consuming. A seller simply does not have the time to run this process themselves.

Moreover, many sellers like the family-office model: they hold companies indefinitely and don't flip in five to seven years like private equity. The caveat is that family offices, in the overwhelming majority of cases, will not even look at deals from an M&A advisor unless they already have a relationship with that advisor - an important consideration when weighing the family office as part of your buyer pool.

A structured and timely process exists when a seller has representation

Time kills deals. When buyers are making multiple acquisitions at the same time, when issues arise that cause a slowdown, or when buyers simply have competing priorities, the timeline extends. M&A advisors force buyers to stick to the timeline.



Building leverage into the deal from the start

Leverage is the most important piece of any transaction. Skilled M&A deal teams continually focus on this from start to finish. **A botched deal can't be fully unwound**: the original buyer pool will know the deal didn't go through, your employees probably have a hint, you have seller fatigue, and by this time the business may have a slowdown in its last-twelve-months' performance. A nine-month exit process now becomes a three-to-five year journey, because what you were originally promised in valuation, terms, and legacy has eroded but you still believe that's the number you think you deserve. M&A advisors mitigate a botched deal from happening as much as possible.

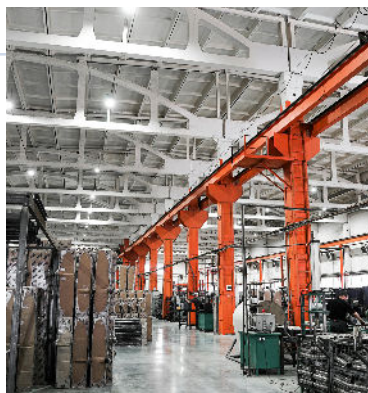
Lastly, a good advisor will strongly advise you conduct a quality of earnings before going to market so that the market has confidence in your books. A great M&A advisor will be willing to split the cost with you.

The LOI

First and foremost know that without M&A advisory representation on your side, buyers submitting unsolicited offers look at LOIs as a placeholder while sellers perceive LOIs as etched in stone. Buyer/seller relationship cracks usually develop here and unfortunately sellers never see the retrade on valuation and terms as a high possibility.

FOCUS Investment Banking's advisors strive to prevent this. We seek to have 93-95% of the deal terms negotiated in the LOI before execution. The below LOI terms are examples of items that have major influence on deal outcome.

- Purchase/sales agreement draft (survival periods, reps and warranties, indemnity caps, etc.),
- Rollover equity draft ("second bite of the apple") exit optionality/timing,
- Employee matters,
- Detailed proof of financing,
- Working capital peg negotiation,
- Who gets compensated for work in progress,
- Addbacks to EBITDA,
- Real estate,
- Sellers note amortization schedules, rates, and term





We make the LOI a very serious point of contention for buyers so that our clients so that the LOI does not become a placeholder and enables the deal to be etched in stone as much as possible prior to close.

Once the LOI is executed maintaining this leverage is critical - all other interested buyers are no longer involved in the process and have to move on. Furthermore, the M&A advisor is responsible for negotiating the LOI, not attorneys. The goal is to pass the LOI off to both parties' attorneys to build in the legalese in the purchase/sale agreement. **The seller gets expert LOI negotiation at no hourly cost (remember M&A advisors are success-fee based) vs. having their attorney do this for them at very expensive hourly rates.**

Moreover, an experienced M&A advisor will artfully call out buyers when their offer is above market with lack of basis provided, particularly if it's not a perfect fit or the buyer hasn't been involved in a bidding war yet. Buyers who are feeling the pressure to make acquisitions often will submit a higher bid, get you into exclusivity, and then retrade the deal downward. It's better to be pragmatic and realistic than naïve.

The Full Deal Team

More experienced sellers or those that have exited before (as well as virtually all buyers) know that M&A advisors, attorneys, accountants, and due diligence teams make up the full deal team. Without an experienced well rounded deal team whose process is quarterbacked by the M&A advisor, leverage is weakened in the process and so is your outcome.

An important point here that you probably have never considered is that when owners contact their financial advisors about an exit, those financial advisors in practice refer you to several M&A advisors for consideration. A financial advisor that tells you to accept an unsolicited offer or to go at it alone would most likely not be providing you with sage advice.

Fees

M&A advisors make the vast majority of their compensation from success fees, as opposed to attorneys who charge a flat hourly rate regardless of whether the deal falls apart the night before close.

Retainers exist to cover hard up-front costs and to keep the seller committed to the process vs. looking for the M&A advisor to do a "market check" or "test the waters" with no intent to close. In other words, M&A advisors can't live off retainers and don't charge hourly rates, therefore incentives for success are deeply aligned.

CONCLUSION FOR POTENTIAL SELLERS OF PRIVATE COMPANIES

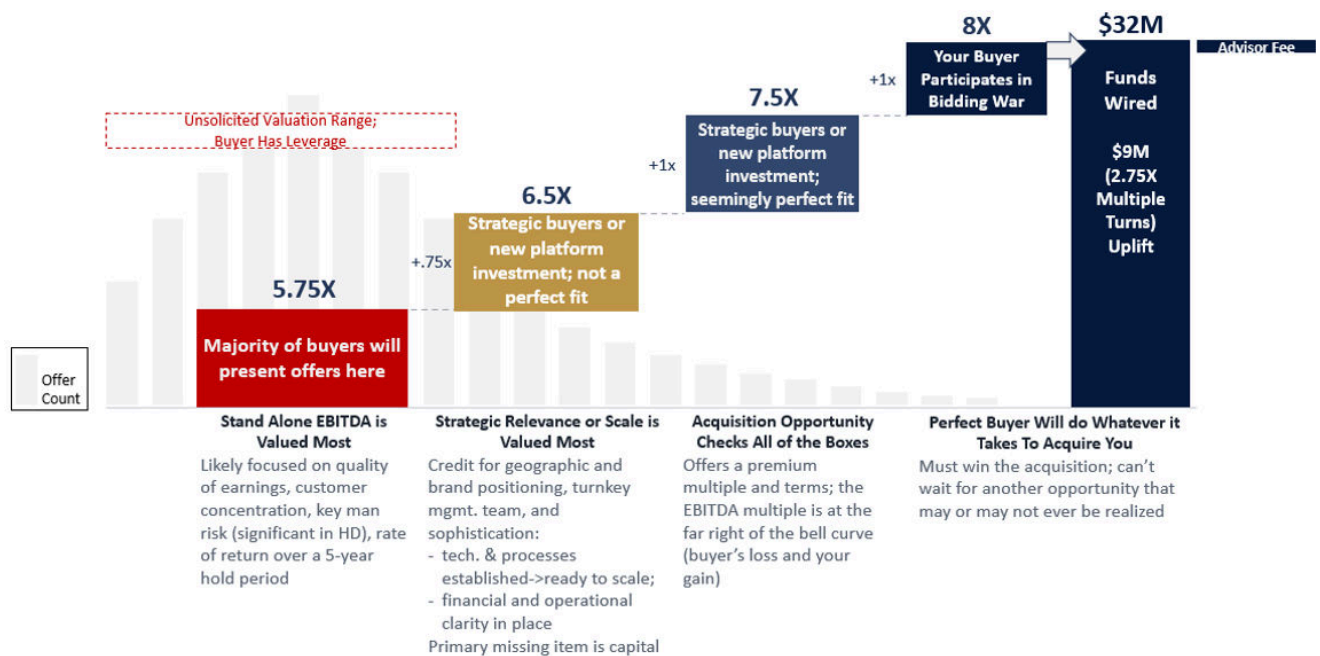
Think deeply about what you want out of your partial or full exit.

Know that if you have an unsolicited offer(s) on the table and accept one without running a full process with representation, you are most likely achieving a suboptimal deal, if a deal at all. The empirical evidence above (that states sellers receive **6% to 25% premiums when using an M&A advisor**) should be taken seriously. Remember the example above: pursuing an unsolicited offer of \$30 million with no M&A advisor could prevent a seller from realizing \$1.8-\$7.5M in additional deal premium or value. The upper end of that is generational wealth for most families.



In many sectors such as heavy truck repair most every business owner is receiving calls, emails, and letters stating that there is an offer on the table for acquisition. Don't quickly fall for the dinner and nice wine, commitments to your legacy, and the sales pitches stating "now or never" or that "this is the best offer you will get" given cultural or strategic fit. Many of these unsolicited offers are from private equity with most owners getting blasted daily. If they can acquire 20 companies for \$100M vs. 15 companies for \$100M, the combined platform EBITDA goes up and their exit in five to seven years becomes much larger. Owners of good businesses don't owe private equity or any other buyer their life's work at a retrospective discount. Be confident about the business you've built, what you deserve, and what the data is telling you so that a premium outcome is realized. **An M&A advisor is your partner in your journey that should be controlled by you.**

Lastly, look at the illustration below using a fictional \$4M EBITDA business that could theoretically have a multiple range between 5-8x EBITDA. Again, this is illustrative and multiples vary significantly by industry. The M&A advisor fee at the top right is a very small sliver of the premium uplift that they generated. Think about what's most important for you, your family, your employees, and your business going forward. My deal team and I are happy to confidentially answer any questions you have on exit strategy.



ABOUT THE AUTHOR



Chandler Kohn
Principal
chandler.kohn@focusbankers.com
803-521-0494

Chandler Kohn is an investment banker with FOCUS's Automotive Aftermarket team, leading the firm's Heavy-Duty Truck Parts and Service industry coverage. He advises clients on M&A and capital raising transactions and hosts Know to Grow: A Light to Heavy-Duty Podcast, which features industry leaders discussing growth and value creation strategies. Prior to joining FOCUS, he was Vice President of Investment Banking at Capstone Financial Group, advising automotive aftermarket companies. Kohn holds a Master of Science in Finance from Tulane University and maintains FINRA Series 63 and 79 licenses.

Source: Agrawal, A., Cooper, T., Lian, Q., & Wang, Q. (2023). "Does Hiring M&A Advisers Matter for Private Sellers?" Quarterly Journal of Finance, 13(1). Sample of 3,281 private-company acquisitions, 1980-2010. Selection bias controlled via Heckman treatment-effect models, two-stage least squares, endogenous switching regressions, Abadie-Imbens matching, and propensity-score matching.