

What Are Buyers Looking For?

By John Jervis, as appeared in *Window and Door Fabricator*

Norm McKibbin and his partner Norm Silberdick, of the **Aspen International Group** have arranged many mergers and acquisitions in the window and door industry. In their experience, what a buyer looks for in a prospective acquisition both parallels and differs from what the seller looks for. Here's what they think moves a buyer most:

Critical mass.

How large is the deal? Larger is generally better, because if there is something wrong, it can be fixed over a bigger denominator (i.e., a problem's effect will be less on a larger company than on a smaller one).

Size.

Companies selling for \$25 million and up are becoming less available in today's merger and activity. Companies in the \$ 8 to \$10 million range will become the new minimum level. Smaller companies can be attractive if they fit into existing management infrastructure or are a strategic regional add-on.

Profitability.

Buyers want the existing company to be profitable. They are not looking for turnarounds unless there is a large discount.

Management.

The people factor is important. The buyer wants a company with a management team that can run the acquired company and execute a business strategy. A company dominated by one individual begs the question of how motivated that person will be after the acquisition (assuming the person stays). Division of labor, good interaction among key managers and cost-effective operation are key factors. While there is often a clean-out of management after an acquisition or merger, it is mostly due to redundancy or weakness.

Strategic thinking and systems.

More often than not, the way to a buyer's heart (and checkbook) is via forecasts, budgets, strategic plans and integrated financial and management reporting systems. Companies with good reporting systems are generally on top of any problems, while those lacking these systems send a message that they're slow to address problems is a real deal killer.

Return on investment.

Surprise! Buyers want to make money. They have a choice of investment opportunities and expect minimum rates of return.

Most buyers calculate investment opportunities using the discounted cash flow internal rate of return method, and they normally expect an annual return of 25% to 30%. The terminal value of the project takes into consideration either refinancing the project or selling it in the fifth year.

Buyers base their offers on multiples of cash flow. Cash flow is defined as earnings before income taxes and depreciation EBITDA (Earnings Before Interest Taxes Depreciation & Amortization) minus recurring capital expenditures. Some buyers use EBITDA rather than EBITDA, with the rationale being the recurring nature of capital expenditures.

Sale prices are usually from four to five times EBITDA. Competitive mergers and acquisitions or special circumstances may drive the price higher (up to seven times EBITDA in rare instances), but the higher multiple lowers the rate of return for the buyer.

In a recent acquisition, a buyer was willing to pay 6.2 times EBITDA to purchase a manufacturer with a broad and diversified customer base in a region the buyer wanted. It also presented an opportunity for the buyer to provide a customer for one of its companies that extruded lineals. The cost savings in materials actually reduced the purchase price multiple to 5.3, which is within acceptable return on investment guidelines.