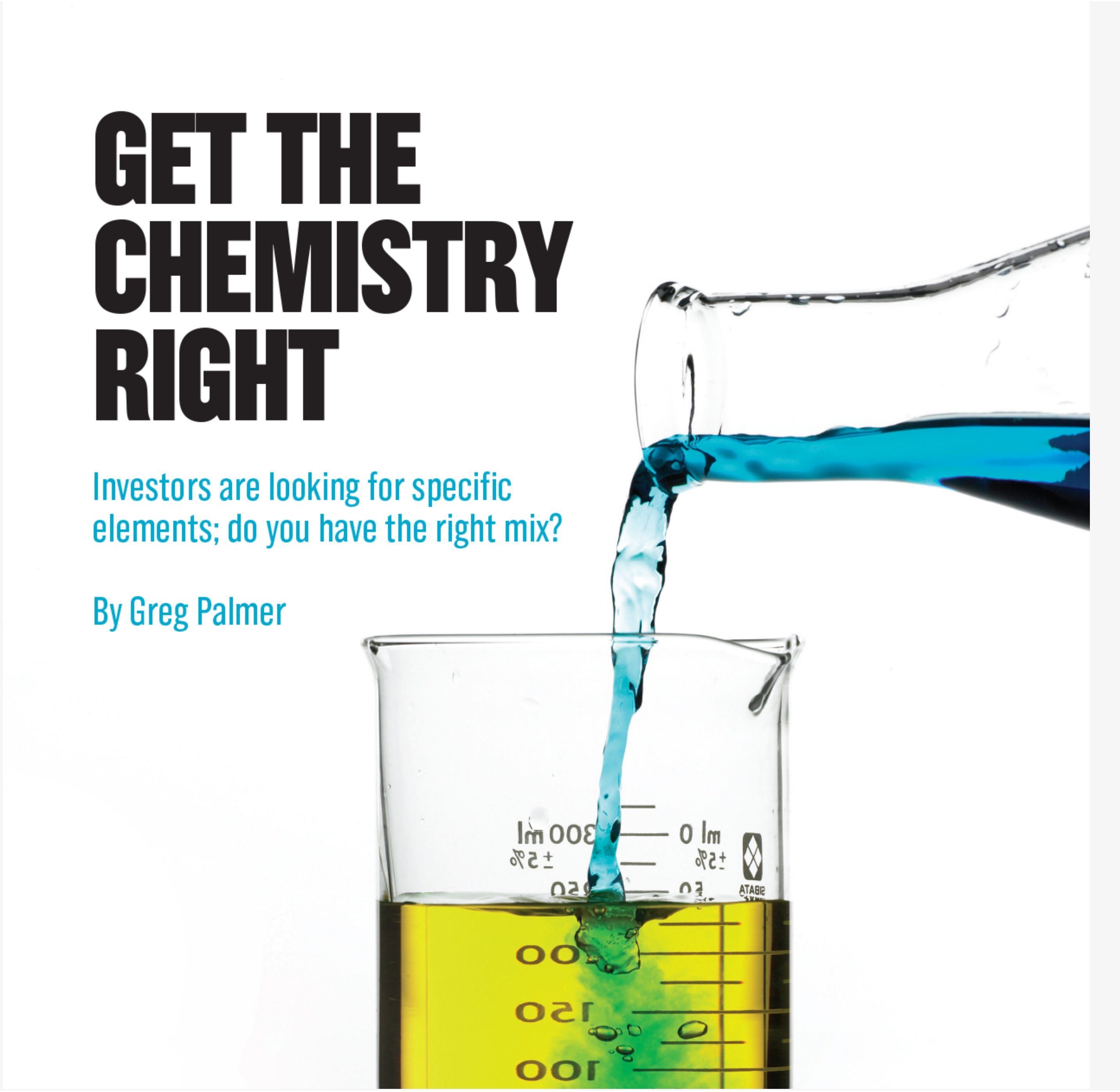

Get The Chemistry Right

Some of the most stressful decisions facing a business owner when considering selling are whom to seek out as a buyer and, of course, how to prepare for such an endeavor. What are investors looking for? Questions such as who would be the right choice to keep the business going once sold or how does one get the most value out of the sale are raised. But who is the right buyer? What is their mindset and why should it matter to you? Here I address some of those concerns.

THE BUYERS

What investors are looking for depends primarily on who the investor is and what they are trying to achieve. Is the investor a financial buyer or a strategic buyer? So in efforts to sell your staffing firm, you must first understand these different buyer targets.

Private equity. Private equity firms used to consider staffing as too cyclical. But in the last few years, more capital has become available. People are looking for investment opportunities. At the same time, the staffing industry has become visible and attractive. With the war for talent heating up, qualified candidates are a hard-to-get resource. The corporate competitive advantage has become talent. Investors have started looking at how they could monetize this shortage.

Private equity firms come in all different shapes and sizes. They can be specialists, generalists, large or small. They typically hold an asset for about five years. They like to see minimum returns of three times the original capital the fund deploys, will almost always put debt on the asset, and usually buy at least a 51% share of the acquired company in order to have ultimate control. These firms often approach sellers with the proposition that they can have “two bites at the apple.” The first bite is the first payment from the buyer. This enables the buyer to take a few chips off the table but roll equity forward, like when Shore Capital bought My Therapy and Michael McBernie the founder sold a controlling interest. It was the same case for Mike Miles, founder of Seaton Corp., when he partnered with private equity and then ultimately sold to True- Blue. The second bite comes when the asset is either recapped or re-sold some time in the future at what is hoped to be a larger amount than the business could achieve on its own, without the additional capital from the private equity firm. This was the case when Miles ultimately sold to TrueBlue and cashed out. This could add up to a less risky path for the sellers. They lose some independence and control; the new partner now owns 51%.

Strategic buyers. There are typically two types of strategic buyers: public and private. Strategic simply means a firm that is already operating in the space.

Public buyer. There are a number of staffing firms in the US and around the world actively looking to acquire staffing firms in the US, as it’s the largest market for staffing in the world and has been a good place to be an acquirer. These acquirers are typically larger firms with more than $1 billion in revenue and several brands or verticals to support. They will typically want to buy 100% of the asset. In this case, there is no “second bite,” but there could be an “earn out” for the seller (a promise for additional payments if certain future financial targets are achieved) to boost the ultimate purchase price. Such was the case recently with public company Cross Country completing the buy-out of private company Mediscan.

Private buyer. There are many private staffing firms that have been acquisitive. Again, they come in all shapes and sizes and with a varied list of needs. The pros and cons of these buyers are diverse depending on the firms, their size and their strategy. Private buyers typically fall under either the private equity category or simply are a private staffing company competitor.

ACQUIRERS' GOALS

There are four main things buyers look for when acquiring a staffing firm.

Growth. The No. 1 item the buyer will be asking themselves is whether the target company can sustain and grow post-closing. Some of their considerations:

Business cycle. Where is the target firm in the macro business cycle — early, middle or late stage? All have implications around potential growth.

Client concentration. What percent of overall revenue do the top 10 or 20 accounts represent? A high revenue concentration means there is risk of going backwards if one or two accounts go away.

Sector concentration. As with client revenue concentration, sector concentration — e.g., financial services, hospitals, construction, automobile — if these sectors are growing or declining.

Infrastructure. Buyers will try to understand the current structure and business model and determine if it can support anticipated growth. They will examine the key areas of IT, key internal staff on the organizational chart, the number of current and anticipated offices and the investments needed to support each.

Opportunities for improvement. Buyers will also look closely for areas for improvement within the target business. Three primary areas they will focus on are:

Revenue growth. Can the business successfully grow the topline? Buyers will look for a plan from the seller to maintain its recent growth at equal or better than market rates. They will examine the seller's specific growth plans for quality and cost. Two good examples of firms that successfully sold and scaled post close with specific plans have been CHG Healthcare and Insight Global in the IT space. They both have proven models that when you add capacity (personnel or new offices), revenue quickly follows and investments have achieved handsome returns.

Gross profit. Buyers will look at the client mix, incentive plans and many other factors in order to find clues for what the future direction likely will be with regard to gross profit percentage. If they discover there is risk in maintaining the current GP%, that hurts value. On the other hand, if they can see ways to improve the GP%, it adds value.

Efficiency. Efficiency is always reviewed. From vendor terms, staff, compensation plans, cost of capital for payroll funding, front- and back-office processes, business model design, use of IT and onboarding of talent — all are considered when making a decision whether the target firm is a viable investment or whether the price is right.

PURPOSE OF THE ACQUISITION

Every buyer is trying to accomplish something with the acquisition. Sellers need to understand what that is.

Expand offerings. Is the buyer trying to enter a new vertical or geographic area? With Medfinders, AMN Healthcare was able to enter the MSP market; TrueBlue entered the workforce productivity category with the recent acquisition of SIMOS.

Talent. The buyer may be searching for new senior talent to add to its existing management team, such as when EmployBridge merged with Select Staffing. The private equity sponsor of Select was interested in adding senior talent so post-close, the newly acquired EmployBridge CEO and CFO were put in charge of the combined entity.

Funding growth. Some buyers are looking for more scale to cover overhead and reduce overall risks, such as when Recruit expanded to the US and around the world, trying to use its platform in Japan as the cash cow to fund growth in faster-growing, less-regulated markets.

Bang for buck. Or perhaps a private equity firm wants to make a bet on a fast-growth category, such as when Snow Phipps bet on the hot healthcare IT segment when it bought HCTec and Partner Professional and combined them to create a fast-growing platform in the space.

More and more, buyers are looking for companies that have systematic programs that help build a strong culture and promote growth of the business. Buyers are looking at net promoter scores, results of best places to work and the tenure of the staff. When Mitsui bought The Delta Companies, these were key considerations. The combination of these items adds up to what the culture is all about.

Sellers should always proceed from informed positions, keeping their options open and run their businesses for the long haul. At the intersection of these two crossroads is where the best transactions occur.

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