Strategic Buyers and Financial Buyers: Do You Know the Difference?

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Know your buyer: it's baseline advice for owners of printing and packaging companies preparing to sell their businesses. This begins with understanding what distinguishes buyers who buy to own from buyers who buy to invest: the two primary categories.

Selling a printing or a packaging business is about more than just pocketing the proceeds – it's also about finding the right steward for your business going forward as you turn the page to the next chapter of your life. That's why it's important to be certain that the business objectives of the buyer are going to align with the seller's personal plans. What those objectives will look like depends strongly upon the type of buyer the seller is dealing with.

There are two broad categories: strategic buyers and financial buyers. At the risk of oversimplifying, we'll say that sellers looking for a relatively quick exit and full compensation at closing may be more properly matched with strategic buyers. Financial buyers, on the other hand, are the right partners for sellers who want to stay engaged in growing the business and are open to retaining an equity stake in it – an arrangement that can pay off nicely if and when the buyer's investment objectives are met.

We advise our selling clients to court both kinds of buyers, making sure that they understand the distinctions between the two types so that they have the luxury of making an educated choice.

Generally speaking, sellers will be more familiar with strategic buyers, who (like themselves) own printing businesses and know the industry well. Strategic buyers' reasons for wanting to acquire other companies are also familiar: for example, to expand the geographical footprint, or to add a capability that the acquiring company doesn't have. Strategic buyers usually hold onto their acquisitions permanently once they've brought them into the fold.

A Breed Apart

Financial buyers are a different breed: well-funded private investors with cash to spend within industries that they may not know particularly well but see as potential sources of high returns. Financial buyers like to build platforms of related businesses through acquisition that they can manage for maximum profitability. Very often, reselling the companies they've acquired is the end-game of their plans.

The nature of the buyer is the key to the terms that will be offered to the seller, especially when it comes to the seller's role after closing.

Strategic buyers will want selling owners to stay on for a transition period of six months to two years, but are typically flexible beyond that. In contrast, a financial buyer will need the expertise of the seller and his or her management team for considerably longer, given that the buyer probably doesn't want to be involved in the day-to-day operation of the business. This is why sellers should expect to put in at least two to three years of active participation after acquisition by a financial buyer.

There also can be a world of difference between the ways sellers are compensated by each type of buyer. In strategic acquisitions, payment in full at closing, or cash and/or earnouts over a set period of time, is a common formula. Sellers don't typically retain any equity – the transfer of ownership is 100%.

But, financial buyers often want sellers to "keep skin in the game" by rolling some of their proceeds into equity. That way, the seller and the management team stay motivated to grow the business and keep pushing it in the direction that the buyer wants it to go. In these situations, the seller often retains 15% to 35% of total equity. Strategic buyers, with their focus on integration and synergy, are less likely to offer equity opportunities to sellers.

One or the Other
Sellers of well-managed, profitable companies can judge for themselves which type of acquisition offers them the best path toward the exit from ownership that they are seeking. For sellers willing to work with financial buyers in shared-equity transactions, the rewards can be substantial.

Not long ago, we arranged for one of our clients to sell the company to a financial buyer, a private equity group, with the client keeping 25% interest. Three years later, with our help, the PE investors sold the company for more than three times the initial purchase price. Our client made more on the second transaction than on the first.

Two other clients, the owners of a flexible packaging company, weren't even interested in offers from strategic clients. Like the first client, they wanted to keep skin in the game by selling the company while retaining equity in it – which they have done, successfully.

We realize that this kind of transaction won't appeal to everyone. It's often a function of age: owners approaching retirement are going to be less excited about retaining an equity stake in the business than younger ones. They prefer to take their proceeds at closing and withdraw at their own pace. Others don't want to deal with the distractions of working for financial buyers who would rely on them both to run the company and to find additional businesses to acquire.

Shedding and Sharing 'Skin'
But, shared-equity deals can be flexible. One of our clients is a retiring owner who has children in the business. The equity that he retains in the sale will go to them, so that the skin in the game becomes theirs. The shareholders of another client worked with their PE buyers to convey an ownership stake to a professional manager they had hired to run the company after their retirement – a rewarding solution for everyone.

These are all good examples to learn from now that the industry is returning to normal after the beating it took from COVID-19. We found that during the pandemic, the financial buyers remained very interested in getting transactions done. They had the funds, and they were hungry for good deals. Strategic buyers, understandably, were likelier to hit the pause button while they steered their own companies safely through the crisis. But the strategics are coming back, finally seeing that long-overdue light at the end of the tunnel.

Given the attractive economic and lending climate we're heading into, we expect there to be more activity by both financial and strategic buyers as companies come onto the market to be acquired. But our advice is, hear every offer out. Weigh the details against personal aspirations, and decide which form of acquisition is going to be more consistent with what the seller wants to do. There's no better basis for making the call than that.

New Direction Partners is an investment banking and financial advisory services formed by Peter Schaefer, Paul Reilly, Jim Russell and Tom Williams to serve the printing and related industries. Services include merger advisory services through the representation of selling shareholders as well as buy side representation, valuation services, financing and refinancing efforts, turnaround and restructuring services, and temporary/interim management consulting. To learn more about New Direction Partners, visit New Direction Partners' website at www.newdirectionpartners.com.