M&A Advisors Proven to Improve Valuations

By Billy Fink, Axial | January 21, 2015

"Do I really need an M&A advisor?" This is a question thousands of business owners ask themselves every year when they embark on the process of selling their company. Although there are many benefits to an advisor, some business owners still choose to bypass the intermediary, thinking the value is overstated.

In an effort to definitively answer this question, several academics "analyzed a sample of 4,468 acquisitions of private sellers during the period of 1980 – 2012 to examine the decision and the consequences of hiring sell-side M&A advisors."

The results bode well for intermediaries.

In the study, entitled Does Hiring M&A Advisors Matter for Private Sellers?, Agrawal et al. discovered that "private sellers receive significantly higher acquisition premiums when they retain M&A advisors." Although "top-tier" intermediaries offered the highest acquisition premium, the benefit of the M&A advisor held true across all deal sizes

M&A Advisors Create Competition

The higher acquisition price derives from an M&A advisor's ability to run smoother processes with better buyer lists. As Agrawal et al. learned, financial intermediaries have "greater economies of specialization and information acquisition, and have lower search costs than their clients." A smooth process means that the M&A advisor is particularly adept at keeping multiple, relevant bidders engaged simultaneously. This concurrent interest from several interested parties is critical to obtaining the best sale price.

"Previous studies find that bargaining power is a significant determinant of the magnitude of private company valuations," wrote the professors. "A key determinant of the seller's bargaining power is the number of competing bids it receives." Like supply and demand, "a seller has more negotiating leverage when a prospective buyer believes that it is competing with other bidders." An M&A advisor helps drive acquisition premium by driving competition.

Best of all, the competition doesn't even need to be real. According to Agrawal et al., the mere presence of an M&A advisor can induce a sense of competition. "An M&A advisor can influence the attitudes and assumptions of bidders. If a seller only has one strategic buyer interested in purchasing the company, using an M&A advisor can give the prospective buyer the impression that there are competing strategic buyers against which it must compete to acquire the seller."

M&A Advisors Are Most Important in Private Transactions

This competition thesis is particularly vital for private companies because of the opacity of the private capital markets and the information asymmetry between first-time sellers and investors.

"Public companies receive more bids than comparable private sellers for several reasons," write Agrawal et al. "First, regular SEC filings allow potential bidders to obtain information about public companies that they may be interested in acquiring without incurring significant costs. Second, public companies tend to have greater visibility and media exposure relative to private firms, increasing the probability that they would attract the attention of potential bidders. Third, a public company receiving an initial takeover bid via a tender offer is required to publicly disclose it. The disclosure is followed by a waiting period imposed by the Williams Act of 1968 to provide opportunities for potential buyers to submit competing bids."

Without these same factors in the private markets, private sellers often benefit from a sense of competition.

Extra-Valuation Benefits

Overall, Agrawal et al. explained, "A sell-side advisor can identify strategic buyers, evaluate the reasonableness of a bidder's offer, manage and pace concurrent negotiations with multiple bidders, reduce the information advantage that a seasoned acquirer has over a private seller regarding the M&A process, and represent a private seller in negotiations with potential buyers."

Although these are extremely compelling reasons to retain an M&A advisor, an effective intermediary can offer benefits beyond price — a good M&A advisor can help a business owner identify the best process for exiting the business. Since many closely-held businesses often experience intense family or shareholder dynamics, which may complicate the transaction, having a full understanding of the available options is essential. For example, if you want to sell the business to family or friends, a management buyout (MBO) or an Employee Stock Ownership Plan (ESOP) may be most appropriate. For transactions involving highly complex family or shareholder dynamics, your advisor can also serve as objective, third-party counsel that helps your business make decisions that maximizes a successful outcome for all stakeholders.

Additionally, advisors help keep you focused on running your business — a vital part of any sales process. They do not let the transaction become a distraction that negatively impacts business performance during such a critical period.