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FEATURE ARTICLE

Win-Win: Ten Secrets to a Successful M&A Negotiation

By Chuck Andrews, CBA

This is an exciting time for M&A transactions – there is a growing number of deals, bankers generally have better financial tools and increased knowledge, and the Internet has accelerated the overall speed and efficiency of M&A dealings.

While the flourishing field of M&A may encourage you to sell your business, there are several questions to ask yourself before selling, including:

- Why are you selling?
- What will you do after you sell?
- Do you have a team of advisors experienced in selling businesses? Will you include them in the planning process?
- Do you understand the importance of obtaining fair market valuation to establish a benchmark for a minimally acceptable transaction?
- Are you focused on cash at closing, or can you understand the value of deal structure and its impact on negotiations?

(article continued on page 3)

EXPERT TIPS

Creating Value Through M&A Transactions

By Ben Howatt, CPA, CVA

Stories in the news media that touch on the challenges of high-profile M&A deals are often quick to conclude that such transactions are failures. Universities and “think tanks” offer little to alter this perception because research results — depending on their source and purpose — tend to be mixed across studies.

On the other hand, M&A has played a key role in the long-term growth and viability of many successful mid-size and large-size companies today. Given that such companies continue to prosper while delivering acceptable returns to owners and investors, it is reasonable to conclude that M&A transactions can create value.

So why the apparent contradiction among media, academia and the corporate arena?

The answer to this question is relatively straightforward: Success is in the eye of the beholder. Success is, to a large extent, defined and measured differently according to each individual’s objectives.

Companies make investment decisions based on the financial and strategic returns they expect to achieve. This is true of buying equipment, adding a salesperson, opening locations or acquiring other businesses.



(article continued on page 4)

TRENDS TO ACT ON

Safer Outlook for Middle Market Banks, New Approaches for Private Equity Groups

By Adam Crutchfield

The credit troubles that have plagued transaction plans for major private equity groups (PEGs) and large investment banks in recent months should not compromise deal activity for middle market banks, according to the Association for Corporate Growth (ACG).

The foremost concern for PEGs at this point is securing the necessary financing for deals that already have been announced. For banks, the foremost concern is tightening rates on such debt. Distanced from credit market activities, middle market investment banks can operate in a safer environment than their bulge-bracket counterparts. While the credit shake-up compromises large banks' ongoing transactions and pipeline to some degree, such concerns do not affect most middle market banks directly. This is because middle market banks do not face the risk of holding billions in committed debt. They also do not hold obligations to introduce additional capital to the market.

Meanwhile, PEGs that are limited in their leveraged finance capabilities are searching for other areas to deploy capital. ACG points out that, given credit concerns now impacting larger markets, the middle market is the likely destination for funds raised by PEGs in recent years. ACG also expects the average size of financial buyer deals to decrease as larger PEGs enter the middle market arena.

“ACG points out that, given credit concerns now impacting larger markets, the middle market is the likely destinations for funds raised by PEGs in recent years.”

EXIT PLANNING

Setting Exit Objectives

By Enrique Brito, CFA, AVA, CM&A

The three principal objectives common to nearly all business owners contemplating a future liquidity event are:

- When it would be the best time to exit the business?
- How much income will you need after you leave the business to maintain your desired lifestyle? Do you expect to be cashed out when you leave the business or are you willing to receive the purchase price in installments over many years?
- To whom do you want to transfer the business? To a child, key employee, co-owner or to a third party who can pay top dollar for the company?

Answering these questions constitutes the first step in the exit planning process. Next, it is important to formulate specific plans to achieve the stated objectives. Business owners are often too focused on their businesses to dedicate a sufficient amount of time and attention to their exit objectives. Moreover, business owners seldom know where to start due to their lack of experience in exit planning. Therefore, begin by working with experienced advisors who can fine tune answers to the questions outlined above, and can guide the planning and execution of additional exit objectives.

For further information on exit planning, please visit The McLean Group's Exit Strategies Institute site at PlanYourExit.org.

FEATURE ARTICLE

Win-Win: Ten Secrets to a Successful M&A Negotiation

(CONTINUED FROM PAGE 1)

Upon the successful conclusion of the outlined analysis, you should understand implicitly the following ten secrets to a successful M&A negotiation:

- 1. Place a Reasonable Price on Your Business**
This is not related to how your business is marketed (with or without an established price), but rather to what you are willing accept as a minimum price.
- 2. Carry On Business as Usual**
Don't become so obsessed with the transaction that your attention wavers from day-to-day demands and affects sales, costs and profits.
- 3. Engage an Expert Intermediary**
An intermediary's focus on confidentiality and effective process becomes the platform for maximizing the transaction's success.
- 4. Prepare for the Sale**
Preparing for the sale well in advance is the most effective negotiating tool for minimizing wasted time, maintaining credibility and shortening due diligence.
- 5. Anticipate Requests the Buyers and their Financing Sources May Require**
This is the first stage of putting yourself in the buyers' shoes.
- 6. Achieve Leverage through Buyer Competition**
A good business, priced properly, will create interest from several buyers and create a competitive situation.
- 7. Be Flexible**
An intermediary should inform you of the areas where flexibility will impact both price and time to close.
- 8. Negotiate – Don't Dominate**
The negotiating process you have used for selling your products and/or services is an asset in understanding the give and take of deals, but the stakes (and emotions) are higher and require a team effort from your advisors.
- 9. Keep Time From Dragging Down The Deal**
To keep the momentum up, work with your advisors to be sure that potential buyers stay on a time schedule, and that offers and counter-offers advance in a timely fashion.
- 10. Be Willing To Stay Involved**
Even if you feel exhausted by the process, realize that the buyer may want you to stay within arm's reach for a while. Consult with your advisors to determine how you can best effect a smooth transition.



It is important to understand the sales process and candidly share your motivations with your advisors to achieve a win-win M&A negotiation. In most cases, buyers and sellers do not immediately walk away from a deal feeling like they have won. The winning feeling usually occurs some months later. What *is* imperative at the closing table is that a fair process was employed, and both the seller's and buyer's needs are satisfied.

EXPERT TIPS

Creating Value Through M&A Transactions

(CONTINUED FROM PAGE 1)

Typically, the acquiring company is simply looking to meet or exceed a set rate of return (hurdle rate) on the new business investment. As long as the acquirer achieves a return that at least equals what could have been earned on the next best investment alternative, then the transaction will be considered a financial success.

Sometimes the acquiring company will sacrifice short-term profitability to pursue long-term objectives. The goal is to remain competitive, viable and profitable; therefore, certain investment choices may be intended to lay a foundation for the future. Under this scenario, an M&A transaction may appear to be a failure based on first, second and/or third year financial performance, while in fact proving successful due to its achievement of key strategic and operational goals.

Further, a true indicator of whether or not an M&A transaction has been successful is how well the combined buyer and target performed as compared to how the buyer would have performed had the transaction not occurred. If there was a downturn in the industry after the deal was consummated (i.e., the tech bust), then this fact must be addressed in the analysis. Similarly, if the company experienced industry-related difficulties or operational problems unrelated to the acquisition, these facts also must be considered.

The news media, on the other hand, is primarily focused on readership, advertising revenues and publication deadlines. Journalists are not fully versed in financial theory and application. Journalists also tend to rely on interviews and third-party research for their stories (including academic sources). As a result, M&A articles commonly overlook strategic and operational motivations, and often do not recognize that an average return does not necessarily imply that a transaction has failed.

The limitations with academic research can result from mismatched comparisons (i.e., “apples and oranges”). Specifically, such studies often compare stock returns realized before the transaction to stock returns realized after the transaction, and/or may compare stock returns among different companies and industries. However, stock prices go up or down for numerous reasons, both known and unknown. In addition, strategic and operational objectives for deals are frequently overlooked in such studies since they are not reflected in the near-term financial performance and stock prices of the acquirers.

What can be done to improve the chances of creating value through M&A transactions?

One implication is clear: if a “growth by acquisition” strategy incorporate criteria similar to those of most inexperienced buyers (or worse yet, is undertaken on a purely knee jerk or opportunistic basis) it is unrealistic to expect to create significant additional value, or to easily achieve acceptable returns on investment.

Even in distressed or bargain situations, the prices of such targets are typically discounted for a valid reason. Only the buyer’s ability to bring something unique to the table will add long-term, above-average returns (but as mentioned earlier, average returns may be satisfactory).

That said, effective planning and deal execution are the key factors in achieving success in M&A transactions.

“Effective planning and deal execution are key factors in achieving success in M&A transactions.”

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Have A Question?

Please submit any topics of interest to egins@mcleanllc.com with the subject: "M&A Market Update Topics" and we will try to address it in the next issue!

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EXPERT TIPS*Creating Value Through M&A Transactions***(CONTINUED FROM PAGE 3)**

A prospective buyer should fully recognize and understand the core competencies of its core business, including strengths and weaknesses, profit drivers, top customers, core vendors and key employees, among other factors. Such strategic planning is critical to determining if and where M&A transactions best fit the company's objectives for growth.

The acquisition plan is then developed as an extension of the strategic plan. Potential targets are identified, ranked, and analyzed, in relationship to how they meet strategic goals. This plan must be flexible and address how to proceed if preferred targets are either not interested or too costly.

As discussions with prospective sellers move forward, the buyer should continuously assess and reassess how well the target fits strategic objectives and meets investment return hurdles. Research, valuation, and due diligence all require appropriate resources and attention.

Finally, integration and transition planning should start prior to closing a transaction. These areas should be addressed at a preliminary level in the acquisition planning stage, then at length during valuation and due diligence.

**THE MCLEAN GROUP'S
SELECT RECENT TRANSACTIONS***Abraxas Acquired By Dauntless**Memphis NetworkX Acquired by CII**Arrowhead Acquired by Caprock***ABOUT THE MCLEAN GROUP**

The McLean Group is a national investment bank providing merger and acquisition (M&A), capital formation, business valuation, litigation support and exit planning services. The McLean Group serves middle market businesses generating up to \$500 million in annual revenues. Headquartered in Washington, DC's technology, communications and government contracting corridor, the firm is among the largest independent middle-market investment banks in the region. The McLean Group is a FINRA Registered Broker Dealer and Member FINRA/SIPC.