WHAT BUYERS LOOK FOR WHEN ACQUIRING A BUSINESS

HOLMES NOBLE

An interview with Simon Hobbs

SIMON HOBBS

Numerous business owners may be contemplating the sale of their businesses yet remain uncertain about which factors hold significance for prospective buyers. In a recent discussion, I had the privilege of hearing the views of Simon Hobbs to gain insights into the key criteria that buyers consider when acquiring a business.

Simon’s most recent role was with Kinaxia Logistics, where he became their first CEO from March 2020 to March 2024. Kinaxia Logistics is a “buy & build business” within the UK Logistics sector and has acquired 14 regional family-owned transport and warehousing businesses.

In his role as CEO, Simon engaged in the integration of these acquired businesses, the assessment of potential acquisitions and he led Kinaxia’s most recent acquisition of Nelson Distribution in September 2023. Prior to joining Kinaxia Logistics in 2020, Simon held senior UK, European and Global leadership roles with Kuehne + Nagel, Ceva Logistics, DHL Supply Chain and Exel Logistics, where he participated in the acquisition, onboarding, and disposal of businesses in Europe and the UK.

There are numerous motivations behind acquisitions. These can include:

- Addressing a service gap, whereby an acquisition supplements an existing service line, as evidenced by Clipper and GXO.
- Market consolidation, exemplified by the current pending acquisition of Wincanton by GXO.
- Acquiring complementary businesses, such as Stobart and Culina or Wincanton and GXO.
- Geographic expansion, enabling entry into previously untapped regions or bolstering national infrastructure, a recent example being Elanders and Kammac.
- Pursuing distressed assets – there are numerous examples of this over the last 12 months within the much-challenged UK transport sector.
- Facilitating a turnaround strategy, highlighted by the creation of YDLGP and their purchase of Yodel.
- Strategic acquisitions, as observed with CMA and Ceva.

When venturing into the acquisition of a business, it is imperative for buyers to grasp the potential for future growth and synergies – where will the value of the acquisition come from?

Hence, the potential for enhancement remains a pivotal focus. In my discussions with Simon, before deeming a business attractive for acquisition, several aspects require meticulous evaluation.

1: Analyse the financial performance of the business.

2: Review all assets and commercial agreements.

3: Consider the quality of the revenue, the operational performance and service levels.

4: Assess the people talent and culture.

5: Understand the expectations and needs of the seller.

6: Identify the quality of Information Technology / Business Systems.

7: Establish how aligned the business is with current market needs.

Financial performance

The financial performance of the business is only one of the areas that determines the value of the business to be acquired. A stellar financial performance is not necessarily the only thing a purchaser is looking for, as the opening “what motivates an acquisition” summarised.

While the current financial performance may be considered as outstanding or acceptable or even poor, the prospect of improvement remains a key driver. How do we deliver value from this acquisition? Acquiring a business that requires a turnaround may be attractive from a purchase price perspective, but this pursuit is not without its risks and acquirers should never underestimate the resources required to achieve this nor the distraction it causes.

My preference has always been to acquire a business that we can squeeze more out of through synergies and operational improvements, or that brings in services we want to develop. I always think twice on potential acquisitions that require a turnaround or that take us into unfamiliar markets.

Asset and Commercial Assessment:

Through our own internal management team, supported by external resources, it is important to scrutinise the business's current assets and identify any impending significant investments that could lead to unexpected costs, particularly around Capex. Some businesses excel at enhancing their assets, but astute investors can see past this. Analysing the cash flow, and future demands on cash, is essential to avoid it draining financial resources.

Also, understanding the business's commercial agreements and contracts, such as property agreements, is essential. Assessing risks to the existing infrastructure, such as leases nearing expiration, is prudent. For instance, having at least 2-3 years left on a warehouse lease is preferable. Furthermore, ensuring any acquired fleet has a balanced age profile, demonstrating regular investment and a replacement program, provides comfort. Ideally, a portion of the fleet, circa 20%, should be under 12 months old.

Revenue Quality:

Stability of income holds immense significance, with buyers seeking clarity on revenue sources and the presence of dominant customers.

Personally, I prefer to avoid individual clients generating over 10% of my revenue, as this could lead to unhealthy dependencies. Relying heavily on a single customer or sector also poses considerable risks, particularly during economic downturns. A balanced income stream across multiple customers and market sectors is the ideal.

In cases where a business does depend on a dominant customer, securing long-term contracts is crucial with any contract-specific assets being co-terminus with the contract term. Ideally, half of the business's revenue should come from repeat and contracted business, with sensible contractual clauses relating to such things as means of annual rate reviews, shared benefit agreements and how to deal with exceptional cost increases – most recently fuel. Any change of ownership clauses also needs to be identified and addressed.

Additionally, assessing existing service levels and gathering customer feedback are vital steps. Understanding the nature and longevity of customer relationships, especially if they solely revolve around the owner, is essential for mitigating post-acquisition risks.

People Talent and Culture:

Cultural alignment stands as the foremost consideration in my evaluation process. Will this potential acquisition fit? A lack of cultural alignment could deter potential buyers. For me, bringing a "poisonous" culture into a business is a definite no-no.

Meeting with the owner / seller provides insight into the dynamics among employees and their engagement levels. I scrutinise the condition of the premises, observing employee interactions to gauge the engagement levels of the workplace. Maintaining high operational and quality standards, especially concerning health and safety protocols, is imperative and can cause major red flags if I can see they are not adhered to.

Assessing talent within the organisation is equally pivotal. I hope to see a strong talent pipeline and understand the availability of a successor should the owner depart. Typically, upon acquisition, I advocate for the owner to transition after 6 -12 months into a Non-Executive Director role, providing occasional guidance while relinquishing day-to-day involvement. Confidence in the capability of the management team to assume leadership responsibilities is paramount. In my experience, leadership teams may harbour self-doubt or imposter syndrome if their professional development has been neglected or if they have been led by an autocratic manager / owner.

Expectations and Needs of the Owner/Seller:

Understanding the emotional stance and strategic objectives of the owner/seller is necessary. Clarity regarding their desire for an exit or a continued involvement post-acquisition is essential. Often, navigating this aspect proves challenging, as differing visions may necessitate significant strategic change, alternative ways of doing things, potential rebranding, and even organisational changes. In some instances, this could entail the departure of extended family members if deemed incapable of fulfilling requisite roles.

Understanding the valuation expectations of the owner/seller is key and can often be the biggest blocker in any sale. While historical trading data provides valuable insights, I also carefully examine projected performance over the next 12 -18 months, especially in challenging economic climates like the present.

Quality of Information Technology / Business Systems:

In addition to the previously mentioned considerations, I also scrutinise various other factors such as technology integration. It is important to comprehend the business's technological landscape, particularly concerning automation and cybersecurity. Assessing the capability of their systems is vital; our internal IT team would determine whether the acquired IT systems can be utilised or if our preferred systems can be integrated without too much disruption. My preference is to implement our existing business systems; this aids the integration of the acquired business and supports standardisation.

Alignment to current Market Needs:

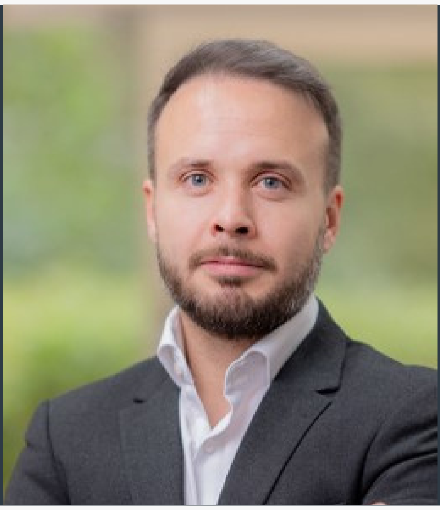
Furthermore, I evaluate the business's stance on sustainability and its awareness of evolving legislation. An appreciation and awareness of sustainability is important in today's business landscape, and compliance with upcoming regulations, such as minimum wage increases, is essential for prospective buyers.

Conclusion:

Buying a business is not just about buying a financially strong performing business. It is about what value the acquisition will bring you and what risks come with it.

For a business owner or leader looking to sell their business, there are numerous factors to consider as outlined in this article. Each of these elements can significantly impact the success of the sale and the financial outcome for the owner.

Holmes Noble Advisory can play an integral role in this journey by providing crucial information and insights that aid the owner's decision-making process. Our team of specialist advisors, available on an interim basis as consultants or Non-Executive Directors (NEDs), are equipped to delve into the business, offering comprehensive support throughout the sale process. From initial valuation to final negotiations, our experts ensure that every aspect is meticulously handled, ultimately facilitating a smooth and profitable sale for the business owner.



Interview by:

TOM GRAHAM

PARTNER GLOBAL LOGISTICS, SUPPLY CHAIN & TRANSPORT

tom.graham@holmesnoble.com

holmesnoble.com