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M&A Statistics: The Rest of the Story

Just-released statistics related to Mergers & Acquisition activity in the third quarter of 2013 are the usual mixed-bag of good news and bad news.

According to CapitalIQ, "Lower middle market transaction volume increased slightly in Q3 2013 compared to Q2 2013, while transaction value increased by 18%. " Well, an increase in transaction value is good news. We all want to reap top dollar for our companies. The slight increase in transaction volume might also indicate that more buyers are coming into the marketplace after years of sitting on the sidelines.

But what's the context here? While the market may have improved from Quarter 2 to Quarter 3, the volume in this market segment during Quarter 3 of 2013 was down 25% from the same quarter in 2012. The big picture matters.

Here's another statistic from Capital IQ that caught my eye because of the mixed message it sends to business owners: "The proportion of M&A deals (in the lower middle market) completed by strategic acquirers increased in relation to financial sponsors. "

Let's look quickly at these two types of buyers. Financial buyers use financial formulas, usually based on a desired rate of return, to determine the price they'll pay for companies. A Private Equity Group (PEG)—unless it is making an acquisition to add on to an existing holding—is a classic example of a financial buyer. A strategic buyer, on the other hand, is one who bases its purchase offer on its perception of the target company's future value: how well it expects the target company to perform under its management, or how successful the acquisition will be once it can take full advantage of the buyer's better market distribution, name recognition or proprietary technology, etc.

Is this increased activity among strategic buyers a glass half-full or half empty for business owners? On the one hand, more strategic buyers in the marketplace improve the possibility of getting more money for one's company. Strategic buyers (competitors, verticals, industry players and adjacencies) are often willing to pay more for a target than are financial buyers.

On the other hand, the financial buyers (often Private Equity Groups) may pay lower prices, but they have deep pockets, bring management expertise to the table and are often the best-possible buyer for owners who want to take some chips off the table, but aren't ready to ride into the sunset quite yet.

I compare statistics in the investment-banking world to beauty: the meaning is in the eye of the beholder. What is statistical good news for one type of business owner (one that wants to raise capital for expansion or sell off some portion of her company to reduce risk) may not be quite as attractive for the owner who wants to sell the entire company for top dollar.

I urge owners of companies in the lower-middle market to use caution when interpreting mega-market statistics. Instead, we should use them to think about how our companies must one day match the requirements of whatever type of buyer is active in that future marketplace. Statistics are simply the background for how we owners will write the last chapter of our business ownership stories: the sale of our companies.

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