

Exits

THE AGONY AND
THE ECSTASY



O'MALLEY
SOROHAN

Learnings from interviews with
20 successful exit stakeholders

May 2019

Background

CONTEXT

O'Malley Sorohan supports high growth, entrepreneurial organisations build the leadership teams they require to deliver on their growth ambitions.

Building out the leadership team is challenging, with many complex decisions along the way regarding when to strengthen the team / what profile / how to incentivise, etc.

Growth ambitions can take on different shapes. For many of our clients with external investors a successful exit is a key requirement.

With this piece of research, we sought to gather insights from stakeholders involved in successful exits, which may be of value to others as they navigate this journey.

INTERVIEWEES



20 People



Mixture of Roles

CEO, CFO, CTO, Head of HR, VC Investor, Acquiror, Board Member, Advisor.

Exit Success

Each has been part of at least one exit of greater than €45m that delivered attractive returns for investors.

SCOPE



Focus was primarily on the technology sector.



Majority of interviewees were involved in Irish company exits to international firms. Interviews also covered broader international transactions with no Irish connection.

Executive Summary

Growth ambitions of companies take many different forms. For most, navigating an exit, for at least some of the shareholders, is both important and challenging. We decided to explore the journeys of successful exits travelled by a range of different stakeholders, to see if their stories could be helpful to our clients as they navigate, or re-navigate, this journey.

Each exit journey was unique, with fascinating nuggets of wisdom emerging from every conversation. We can't disclose the sensitive and confidential nature of the specific journeys or condense the full richness of these stories into a few pages. However, we have distilled our learnings into a set of common themes that cut across the different stories. Not surprisingly, given that we are in the executive search business, these learnings don't address the mechanics of the financial transaction, but rather the broader people related factors involved in determining exit readiness.

While each exit is different, the motivation and experience of both the buyer and the seller, and the mismatches that happen here, can be key determinants of the exit journey and outcome. The most successful exits seem to correlate with situations when there was a match (or probably more importantly a perceived match) in both the interest level of both parties and the exit process understanding of both parties. Interestingly, mismatches which appear initially advantageous to one side, frequently create issues at a later stage for both sides.

Successful exits are rare, with the majority of businesses failing to get the exit they target. Success when it comes, comes at a price, typically involving significant demands of key business leaders. Building resilience in ahead of time is critical in order to stay the course.

Indeed, what 'success' means can also be problematic. Lack of alignment of stakeholders is a frequent issue and requires careful construct and communication. Clear alignment at an early stage is essential to enable the cohesiveness required during the typically charged atmosphere of an exit.

All interviewees discussed **the necessity of surrounding themselves with great people – executives, board members, advisors. However, defining 'great' was trickier.** 'Great' changes with stage of growth, ambitions, sector, function and compromises may sometimes be required. The one area where compromise was universally ill-advised was a fit with values.

There was an interesting divergence of opinion on the degree of focus on an exit that was appropriate for a company. Getting the right balance on long-term business building, while preparing for a potential exit is clearly a delicate tight-rope walk.

The buyer's risk paradox was fascinating. Prospective buyers are often initially attracted to the innovative, fast-moving culture of an entrepreneurial high growth business. But when it comes to closing the deal, those same buyers typically also want a 'plc' attitude to risk, reporting and procedures. The two rarely go together. Successfully negotiating a sale (or more difficult again, an integration into a larger, more mature business) takes a lot of thought.

Finally, whilst exits are clearly challenging they can also be rewarding on many fronts, and for many highly addictive.

We hope these insights stimulate your thinking with regard to your exit readiness.

Key Learnings



ALL EXITS DIFFERENT,
BUT EXPERIENCE AND
MOTIVATION KEY
DETERMINING FACTORS



PROBABILITY
OF SUCCESSFUL
EXIT LOW, AND OFTEN
COMES AT A PRICE



DEFINITION OF
SUCCESS VARIES,
AND **ALIGNMENT**
CAN BE TRICKY



RIGHT TEAM
CREATES REAL VALUE,
BUT "RIGHT" IS ALL
CONTEXTUAL



RIGHT TEAM NOT JUST
ABOUT EXECUTIVES,
BOARD AND ADVISOR
SELECTION ALSO CRITICAL



GETTING THE RIGHT
EXIT FOCUS IS A
DELICATE BALANCE



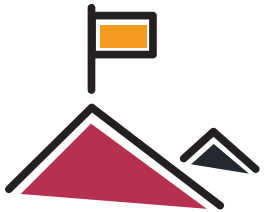
BUYER'S RISK PARADOX:
RISK-TAKING BOTH THE
PROPOSITION AND
THE LIABILITY



EXIT SUCCESS
HIGHLY **ADDICTIVE**



ALL EXITS DIFFERENT, BUT EXPERIENCE AND MOTIVATION KEY DETERMINING FACTORS



We set out to identify a set of principles that applied to all exits. But it quickly became clear all exits are very different.

“

I've been involved in 25 different exits in some capacity and the one thing that they have in common is that they are all different!”

- **VC investor**

“I'm very wary of working with a business where key individuals have prior experience of just one common exit, as they expect to replicate this experience. The more exits you see the more you know to expect the unexpected.”

- **Financial advisor**

“I've been through 2 exits to date – I thought second one may come easier, but ended out been so much more challenging.”

- **CEO**



Many different dimensions that may dictate the shape of an exit, but prior experience and motivation of both buyer and seller are key determinants of both the journey and the outcome.

EXPERIENCE



Buyer

- Number of previous acquisitions overall, and in particular comparable exits (size/geography/sector).



Seller

- Experience of navigating exit process within this organisation and others.

"Initially I thought we were dealing with a **sophisticated buyer** that had a lot of M&A experience. But they had **no prior tech** experience which resulted in huge **challenges** in the due diligence process, earn-out construction and eventually a slow-death integration."

- **ExCo Member**

"Both sides get how this works – it becomes a **game of grand master chess**, with motivation on both sides being a key determinant of the outcome."

- **Financial Advisor**



"Can be a very tricky process, with the pitfalls many and varied, including **an unhealthy, uncomfortable dependence on lawyers** – never again!"

- **CEO & Founder**

"In hindsight I realise how much we **left on the table**, we had no clue how to set up the business for sale, and simply got caught up in **the initial excitement and eventual chaos** of being approached with an offer."

- **CEO**



Motivations of both buyer and seller are key determinants of the outcome - particularly when mismatches occur:

MOTIVATION



Buyer

- Importance of completing now
- What is the buyer looking for from this acquisition:
IP/Fill product gap/
Talent/New markets/
Signal to investors.



Seller

- Importance of completing now
- Credible options open to them:
Other acquirors/
Funding/Going it alone.

"They knew we had to sell, **we played our cards too open and too early**, and they were in no hurry. We left a lot on the table."

- **Founder**

"We loved the product and the team, and they could see the value we could bring to them. **It was all so seamless** – the deal was done in a matter of weeks."

- **Acquiror**

SELLER MOTIVATION

SELLER BEWARE

Seller more motivated. Buyer calls the shots

TRUE LOVE

Buyer and seller motivation aligned

BLIND ALLEY

Buyer and seller not motivated

SELLER POWER

Buyer more motivated. Seller calls the shots

BUYER MOTIVATION

"There was an **immediate distrust** between both CEOs. On paper it looked like a great match, but the cracks soon emerged."

- **Advisor**

"Our IP was crucial to their product and others in the market and we knew it – **we played it well.**"

- **CFO**



PROBABILITY OF SUCCESSFUL EXIT LOW, AND OFTEN COMES AT A PRICE

**Successful exits are rare and
challenging to deliver ...**

Majority of businesses don't get the
exit they originally targeted

While it is hard to measure whether
investors get what they want, at a very basic
level this 2018 data highlights a disparity.

¹ IVCA Pulse report

² Data extracted from Investec 2018 'Review of Irish trade sales, buyouts and acquisition'.
Note transaction value not disclosed in all so this is an estimate.



VC INVESTMENTS

114 companies raised
VC investment in
Ireland in 2018¹



EXITS

10 exits greater than €20m
for tech/life sciences
companies in Ireland in 2018²

Majority of exit processes don't
result in a transaction



"Less than 50% of processes
where a company has engaged
with a potential buyer, resulted
in a transaction."

- **VC Investor**



"Not unusual for one company
to engage with 3-4 exit
processes before final
success."

- **Financial Advisor**



... and when success comes, it often comes at a price.

Exit process longer and more challenging
than everyone envisages

- In over 70% of the cases we discussed, the process lasted longer than 6 months from initial engagement with buyer to close.
- Exit process length ranged from 5 days to 7 years.

Hugely demanding on leadership team –
particularly the CEO and CFO

- CEOs interviewed typically invested 50%+ of time in exit process, CFOs often more.
- Very difficult to manage exit process whilst delivering on day to day business.



" Plan for a **2 year focused programme** – preparing, positioning and then executing."

- **CFO & Financial Advisor**

" In one client we worked with, the initial approach included a €200m offer, company sold to same buyer **7 years later** for €7m."

- **Financial Advisor**

" We went all out to deliver the sale, with huge demands on the company, myself and my family. When it failed, it took a **long time to pick ourselves up** and dust it off."

- **Founder**



**IT IS IMPORTANT TO ENSURE THE
TEAM HAS THE RESILIENCE REQUIRED
TO DELIVER EFFECTIVELY.**



DEFINITION OF SUCCESS VARIES, AND **ALIGNMENT** CAN BE TRICKY



**Success means very different
things to different people ...**

Success definition from a shareholder perspective

FINANCIAL

- Depends on the stakeholder and depends on their expectations (and experience!).
- How much value is left on the table.

EMOTIONAL

- Getting out, before burn out.
- Importance of public recognition.

... and from an employee perspective

FINANCIAL

- If they have shares / options, an exit may be very attractive. However pay-out may not be the dream they had bought into.
- If they don't have shares / options, employees may feel disgruntled about being left out.

EMOTIONAL

- Burn out – particularly if timing of exit not what had originally planned for.
- Some employees may not have bought fully into the exit and feel let down by the founder who “sells out” - particularly if the acquiror is a competitor.

Understanding of “finishing line” also varies

- Getting to term sheet
- Getting to closure
- Earn-out



... and getting alignment among stakeholders is tricky but crucial.

Incentives can help alignment

- Differences of opinion regarding how broad to spread the wealth generation.

1.

Make sure everyone in organisation shares in some of the value

- Everyone in organisation plays a role – it's hard to create collaborative culture if there is an 'us' and 'them' divide.
- From day 1, bring in expertise to ensure architecture and management of incentive process makes sense and is aligned with business needs.

VS

2.

Limit to key people

- End up sharing value with people that don't value it.
- Can often create dissatisfaction, if it's not the windfall they expected.
- Managing exit process can be challenging if broad sign off required.

Keep the circle of who is in the loop extremely tight

- Throughout the exit process, it's important to keep as few people in the loop as possible – most interviewees advocated for restricting initial engagement to just CEO and CFO.
- At some stage other key individuals will need to be engaged, but be clear regarding expectations of outcome.



" We have all shed blood, sweat and tears over the last 10 years, **everyone needed to be part of the party.**"

- **CEO**

" Failed exit like **introducing drugs** into a football team."

- **Investor**

" **Restrict exit knowledge** from spouses / families as long as possible. If family start to get excited, wrong decisions can be made. That can put a lot of pressure on business to stay in a process that they should walk away from."

- **Investor**



RIGHT TEAM CREATES REAL VALUE, BUT “RIGHT” IS ALL CONTEXTUAL



Even a very strong team can't succeed if product and/or timing wrong. But the right team can make a real difference to both the journey and the final size of prize.

Attracting acquiror interest often requires strengthening of the leadership team

- Timing of leadership change is critical to consider - you can be too late OR too early.

Strength of executive team beyond the CEO is particularly important at exit time

- Strong CEO (very frequently a founder) is essential to building a business.
- However overreliance on CEO can often be the biggest barrier to exit.
- Acquiror needs to know that business is more than 1 person
 - particularly as it's highly likely that CEO will not remain in the business post exit.
- Business needs to be able to deliver on day to day performance, while CEO is managing the exit process.



“Increasingly, acquirors are becoming **more focused on team strength** and more rigorous regarding how they assess this. There is a global war for talent and a prime motivation for acquisition is often around talent.”

- **Investor/Board Member**



"From an acquiror point of view, **people is hardest thing to solve for.**"

- **Acquiror**

"Most companies build leadership capacity in arrears – slightly later than needed. As a result, there is little capacity to deal with unexpected, and CEO burn out is high. If you **build team capability ahead of growth**, then you have time to step back to think strategically."

- **Investor**

"**Figure out what capability you are selling** and how you can convince the buyer that this will be retained."

- **Acquiror**





Getting it 'right' requires consideration of multiple dimensions and will change with time.

Getting it 'right' requires looking at multiple dimensions for each individual ...

- **Experience**
- **Commitment**
- **Values/Culture**
- **Connection**
- **Motivation**



"Investors often want to **over-emphasise experience**. But in my view, in early hires, motivation is the single biggest factor."

- **Founder**



... and getting the right structure

- Right span of control at each level.
- Regional vs functional.
- Within functions – e.g. how to structure hunter/farmer element of sales?



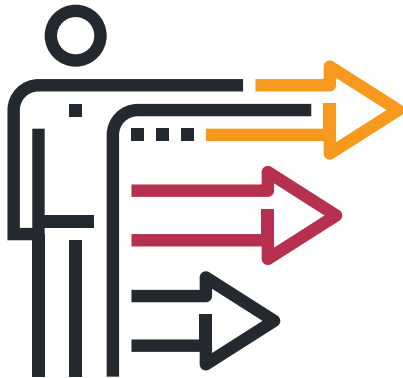
... and right performance management

- Communicating clearly and consistently.
- Getting the right balance between collaboration and accountability.
- Managing the inevitable culture clashes within the business, as it grows and expands.



.... and making the 'right' changes with time

- Make, and follow through on, timely people decisions.
- Important to consider what titles you give people – as may need to bring in a senior hire above a less experienced hire in time.



“

“Every hiring mistake I ever made came back to **over-looking poor values fit.**”

- CEO

“Fire someone the minute you think about it – **it never works out.**”

- CEO

“During first few years we tended to hire junior people as concerned about costs, but often expected them to have too broad a role. Then we **over promoted/over promised,** creating serious problems that had to be unravelled eventually.”

- HR



RIGHT TEAM NOT JUST ABOUT EXECUTIVES, **BOARD AND ADVISOR SELECTION** ALSO CRITICAL

Board composition and advisor selection is important to enable informed strategic and tactical decision making, but also to provide the emotional support to CEO and team during the roller coaster journey.



"Exiters typically **don't know what they don't know** – that's the challenge and the opportunity as an acquirer."

- *CFO & Financial Advisor*





Board composition

- Require a number of individuals who have each experienced two or more exits. They understand some of the pitfalls and are not overly swayed by single successful experience.
- Key non-execs can give advice, but also play a role as a trusted confidant that the CEO can vent / brainstorm with during process.



" Board member with **deep understanding of PE mentality** played key role in preparing for successful PE exit. He was able to highlight areas where we should cut costs as PE buyer would not value."

- **CEO**

Advisor selection

- No matter what experience you have in executive / non-exec team – none will match the breadth of experience available from advisors.
- The more experienced the CEO / CFO in our interviews, the more they valued strong advisors.
- Choose the right advisors and bring them in early.



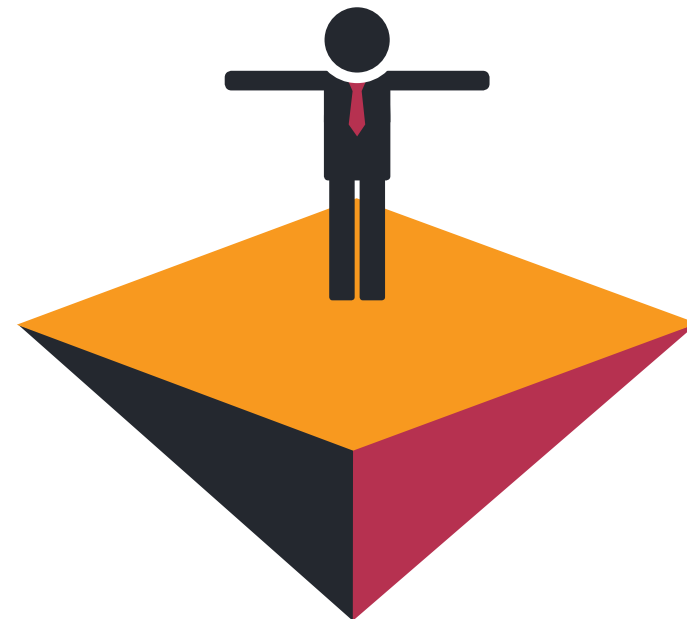
" I wish we had brought in a sell side consultant 18 months earlier to do due diligence on company – so they could help us **focus** on what would add most **value**."

- **Experienced Investor**



GETTING THE RIGHT EXIT FOCUS IS A **DELICATE BALANCE**

All investors will require an exit at some stage, and therefore enabling a successful exit is a key requirement of many CEOs. However interviews highlighted the dangers of building a team that is solely focused on a narrow set of exit options.





SOME OF THE PITFALLS OF BEING TOO EXIT FOCUSED

Single buyer dependency

“We were focusing on building a team that would be a nuisance to our target acquiror, and we didn't focus on the rest of the market. When our target acquiror bought a different player in the sector, we had to start building out a full sales function. But at this stage other competitors had started to create a foothold, slowing our growth and increasing the cost of customer acquisition”

Inhibiting Scalability

“We set out to meet the needs of different customers – delivering bespoke solutions to meet their needs. Our customer list impressed potential buyers and resulted in a sale. This came to haunt us however during earnout period, when we couldn't deliver on scaling targets without a scalable product – we were essentially a professional services business.”

Exit Timing Dependency

“The buyer got a sense that the company was under pressure to close. They slowed everything down believing that we would accept a lower valuation in time. We started considering alternative options and the process picked up again”

“A ‘For Sale’ sign is like waving a white flag giving all the power to the buyer. It only works if you are very confident of a large number of buyers ready to move quickly.”



Getting the right exit focus is a delicate balance and opinions varied on what is the right level of focus – it's a challenging tightrope walk.



“ BUILD A BUSINESS THAT WILL RUN FOR EVER, BUT BE READY TO SELL TOMORROW”

“

“ I never want to hear my companies focused on exit – there are too many things they can't control.”

- Investor

“ Cannot start thinking on proposition and acquiror targets too early.”

- Investor

“ Exit plans typically don't evolve as planned – I don't want a CEO / team disillusioned if they don't achieve initial plan.”

- Investor

“ Exit lens more important for product decisions than people decisions – when making product decisions you are looking to ensure that product gets attention of possible acquirors and will become pebble in their shoe / fill gap.”

- CEO

“ Must have understanding of exit options from very early stage – constantly updated and needs to be broad. However critical to have viable stand alone plan in place throughout.”

- CFO

“ One of our board members asked us every month ... what are your exit options? Who would buy you tomorrow, in 18 months, why? It was his way of keeping us open but focussed.”

- CFO



BUYER'S RISK PARADOX - RISK-TAKING BOTH THE PROPOSITION AND THE LIABILITY



Buyer's interest in a smaller company is often based on the culture and track record of taking risks. However in order to close the transaction, the buyer due diligence focuses on ensuring no/low risk exposure. Seller needs to understand this risk paradox and address both stories.

Buyer's interest in risk taking

- IP/Product that has been brought to life by an organisation that has taken risks, that larger buyer cannot take in pursuing risky innovations.
- Organisation culture / talent that is more nimble, entrepreneurial. Important to think through how seller can portray this culture to acquirors.

Buyer's risk aversion

Buyer due diligence process focused on ensuring that story is robust with no risks:

- Financial forecasts that are accurate.
- HR processes that are water-tight.
- Contracts / legals water-tight.
- Management references need to be squeaky clean.



"Buyer often **looking for the impossible** ... a dynamic, risk taking, nimble business, that has the processes and controls of a plc."

- **Financial Advisor**



"A culture of **agility, speed & passion** of huge importance – we looked at build vs buy and couldn't build that culture."

- **Acquiror**



EXIT SUCCESS HIGHLY **ADDICTIVE**

Exit process is challenging, but clearly also rewarding on many fronts and for many it is highly addictive.

Every interviewee we talked with has continued to pursue subsequent exits in some capacity following their initial exit experience.

“

At the time of sale I promised myself and my family that would never go through this again, but **here I am again.**”

- **CEO**

“ Fifth time around and still get the most incredible **buzz** to get a sale over the line.”

- **CFO**

“ Sitting in lawyer’s office late at night, waiting for final legal agreement to come through is a **weird and wonderful feeling.**”

- **CEO**

“ As a CEO, I enjoyed the **roller coaster ride** of building and selling my business. I’m not ready to take on that again but can’t walk away completely. I feel privileged to play a role as an investor / board member in multiple transactions since.”

- **CEO/Investor**

“ One of my favourite memories was that teleconference with the broader leadership team, as I explained they all had just received an email detailing the amount they had earned as a result of the sale.”

- **CEO**

“ Each and every transaction has its challenges, but I get a great feeling when I can support a founder **realise his dream.**”

- **Financial Advisor**

Exits: The Agony and the Ecstasy – A Review



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IS YOUR TEAM EXIT READY?



What's your team's exit readiness score?

If you would like to
discuss give us a call.

1

Does your organisation have the functional and scaling expertise to deliver the growth story to underpin a strong exit?

2

How does your collective exit experience (within exec & non exec team) compare against potential acquirors' experience?

3

How confident are you in the fit between each of your senior team members and your business needs – not purely skills and experience, but also values and motivation?

4

Do you understand how your business structure may need to evolve or change to deliver on growth / exit requirements?

5

Does your team have the capacity and resilience to go through the exit process, including the possibility of multiple failed exits before a successful completion?

6

Do you have right the combination of skills, experience, values, motivation and governance expertise at board level?

7

Have you engaged the right advisors to fill expertise and experience gaps through the various stages of the exit process?

**O'MALLEY
SOROHAN**

We understand
high-growth businesses.

We understand **entrepreneurial
business leaders.**

Our expertise is in
match-making the two.

www.omalleysorohan.com