

PRIVATELY-HELD COMPANIES EXPECT MERGERS, ACQUISITIONS AND STRATEGIC ALLIANCES TO DRIVE NEW GROWTH, SURVEY FINDS

NEARLY HALF OF MID-MARKET FIRMS WILL CONSIDER BUYING OR SELLING; EVEN MORE WILL CONSIDER STRATEGIC ALLIANCES IN THE NEXT YEAR

Privately-held U.S. companies expect to rely increasingly on mergers and acquisitions as a means of growing their companies, according to a survey conducted by middle-market M&A advisory and management consulting firm **Bywater Inc.** The survey of companies with revenues ranging between \$5 million and \$100 million found that 48 percent are considering acquiring other firms or selling some or all of their existing businesses. Another 3 percent are not actively considering deals but would be "receptive to discussions," respondents said. In contrast, 59 percent of companies surveyed said they have not made any acquisitions since the beginning of 1998.

SMALL COMPANIES WANT GROWTH, TOO

36% are aggressively seeking growth
38% are actively seeking growth
21% are opportunistically seeking growth
5% are not seeking growth

Source: Bywater Executive Survey on Growth Trends at Privately-Held Companies

The study, conducted with assistance from Yale University and Quinnipiac University, was conducted to better understand the attitudes of privately-held firms. Little information on this topic currently exists, according to Kevin Fiala, principal of Bywater's Corporate Development Services division. "Recent reports in the M&A industry indicate that privately-held companies represent approximately 85 percent of all mid-market companies sold. Our Growth Survey underscores the vital role privately-held companies play in the M&A middle-market, but also reveals the lack of understanding that exists about this important group of companies," Fiala is quoted in a company press release.

'Privately-held companies represent approximately 85 percent of all mid-market companies sold.'

More than 100 top executives, including CEOs, owners, presidents, and board chairs of privately owned companies contributed to the survey. Seventy-three percent of responding companies have annual revenues of \$5 million to \$49 million. The survey included both high-tech and traditional manufacturing and services firms, but excluded firms whose business is primarily retail.

Firms Predict Limited Growth

Even though more companies say they are considering

acquisitions to drive growth, the majority (53 percent) projected very conservative year-over-year revenue growth of 4 percent or less for July 2001 through June 2000. The survey was conducted before the terrorist attacks of Sept. 11. Follow-up research will try to ascertain the impact those events dealt the economy on the firms' projections. Fiala acknowledges that the economy was in poor shape prior to Sept. 11, and thinks that may account for the modest projections. Anecdotally, he notes that in conversations since that date, opinions fall into two camps. Some who were "on the fence" about selling may have decided that this a good time to get out. On the other hand, some may see declining valuations as a reason to postpone selling, Fiala said.

"Almost three quarters of the companies said they want to grow, but they only projected a small amount of growth for the most part, and that means that there's some gap. They want to grow, but they can't. So what does that mean?" Fiala asks.

'They want to grow, but they can't.'

Private Firms Want Alliances

Perhaps surprisingly, a higher percentage of the companies surveyed are considering strategic alliances. Seventy-three percent are considering or strongly considering alliances, versus the 48 percent considering a purchase or sale.

Alliances are "Very much an interest to a lot of the mid-size and small companies because it gives them an alternative for growth without an acquisition or merger," Fiala said. "You get some of the benefits, but you don't get all the baggage that sometimes comes along with an acquisition." Many may also see alliances as a viable alternative for generating growth if they don't have the financial capability to do an acquisition, he said. And once accompany has had one successful experience with a strategic

'Multiples are down on privately held companies, so if you have cash and you're a buyer, it's a great time.'

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PRIVATELY HELD FIRMS VIEW STRATEGIC ALLIANCES AS AVENUE TO GROWTH

57% are strongly considering alliances
16% are considering alliances
3% aren't proactively considering alliances, but are receptive to discussions
24% are not considering alliances

Source: Bywater Executive Survey on Growth Trends at Privately-Held Companies

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acquisition, they're likely to do it again. "Most of the small-to-mid-size businesses that we talk to, if they're not involved in alliances, they're thinking about it, and if they are doing one, they're thinking about another," Fiala said.

Although the initial survey did not examine attitudes by industry, Fiala believes that the level of interest in mergers and acquisitions is driven in large part by what's happening within a specific industry. "Certain industries are consolidating, and that may prompt people to think about it," he said. Fiala also thinks some of the interest in buying or selling is driven by the need for

WHY PRIVATELY-HELD FIRMS NEED CAPITAL

41%	Growth capital
22%	Strategic initiatives
19%	Ongoing liquidity
8%	Immediate liquidity
8%	Ownership and generational transitions
2%	Globalization

Source: Bywater Executive Survey on Growth Trends at Privately-Held Companies

growth in a weak economy, where it may not be possible to attain desired growth organically. Just 40 percent of the survey's respondents said they expected to grow primarily through

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organic efforts – new products, increased sales, etc. – while 26 percent expect to achieve their goals externally through M&A, alliances and joint ventures. Nearly 30 percent said growth would be equally weighted between organic and external methods. Follow-ups to the original survey will attempt to examine the results by industry, Fiala said.

Nearly half of the privately-held firms say they will look to international expansion of their businesses to drive growth in the year ahead. Twenty-five percent said international growth was "extremely" important, while another 23 percent recognize it as an important component of future growth. Slightly more than half — 52 percent — said international expansion was not an important part of their growth plans.

New Products, Services Drive Growth, Too

The privately-held firms don't plan to rely on deals and alliances alone for growth, the study found. Developing new

FEW RECENT ACQUIRERS AMONG PRIVATELY-HELD COMPANIES

How many acquisitions has your company made since the beginning of 1998?

None	59%
One	23%
Two.....	6%
Three	5%
Four	2%
Five or more	5%

Source: Bywater Executive Survey on Growth Trends at Privately-Held Companies

products was seen as a key to organic growth; 88 percent of survey participants said they plan to release new products or services during the next 12 months. Fifty-one percent plan to create new products/services that either focus on revenue enhancement or cost reduction.

The new product development process, however, is not given enough attention, with only 50 percent of surveyed companies claiming they have an adequate and formally documented new product/service development plan with clear ROI/value creation thresholds.

Twenty-six percent expect to achieve their (growth) goals externally through M&A, alliances and joint ventures.

One area that concerns Fiala is the lack of strategic planning among privately held companies.

MANY FIRMS HAVEN'T PLANNED FOR M&A INTEGRATION

Does your company have an adequate current strategy for post-merger or post-acquisition strategy?

Yes	41%
No	59%

Source: Bywater Executive Survey on Growth Trends at Privately-Held Companies

"There isn't a tremendous amount of strategic planning that's done among the private companies; only 55 percent say they have an adequate and documented strategic plan. That's a concern ... There is some correlation to having a strategic plan and achieving high growth," he said. It's one of the areas Bywater expects to focus on in follow-up studies.

A detailed follow-on qualitative study is planned, then Bywater expects to package and sell the survey results, Fiala said. ☞

M&A Web Link: For more information, visit www.bywater-consulting.com