



Study

What Do Buyers Look for When Purchasing a Business?

Understanding the Canadian
Market to Successfully Buy
or Sell Your Company

November 2017



Table of contents

Highlights 1

Context 2

1. Profile and characteristics of entrepreneurs
looking to acquire an SME 3

2. Motivations of buyers and types of businesses sought 9

How to avoid getting burned when buying a business 12

Bison Fire Protection:
Lessons learned from a string of acquisitions 14

Conclusion 15

Survey methodology 16

Author

Sylvie Ratté, Senior Economist

Acknowledgements

We would like to thank Tom Corner, Isabelle Simard, Marco Santos Pires, Benoit Mignacco and Don Macdonald for their valuable contribution in conducting this study.

This research was prepared by the Economic Analysis team from Marketing and Public Affairs at the Business Development Bank of Canada (BDC). It is based on public and proprietary data that was analyzed and interpreted by BDC. Any error or omission is BDC's sole responsibility. Reliance on and use of the information herein is the reader's responsibility.

Copyright © 2017 Business Development Bank of Canada

1 888 INFO BDC | bdc.ca

Highlights

19%

Nearly one in five entrepreneurs intends to acquire another company in the next five years.

- This report follows the September 2017 study, *The Coming Wave of Business Transitions in Canada*, which looked at the sales intentions of Canadian business leaders. As few studies have addressed the buyer's perspective on this issue, this study aims to fill that gap.
- The study finds that nearly one in five (19%) entrepreneurs intends to acquire another company in the next five years.
- These potential buyers have a high propensity to grow (84%) and take risks (63%). Not surprisingly, they are among the most dynamic business owners in our country.
- Acquiring a competitor tops the list of buyer motivations. Buyers are looking primarily for companies the same size or smaller than their own, with good profitability. Overall, these findings apply regardless of the potential buyer's size or propensity to grow and take risks.
- More buyers are looking for stable businesses (61%) and growing companies (31%). A warning to sellers: Very few buyers (8%) are looking for unprofitable businesses or companies in decline (i.e., companies they will have to turn around before they can start reaping the benefits).
- A wave of consolidation appears to be emerging. Among business leaders with 20 or more employees, 44% expect to acquire another company over the next five years. This wave of consolidation bodes well for the economy as it could allow for the emergence of Canadian businesses that are in a better position to compete in international markets.
- For the Canadian economy, the upcoming management changes among Canadian companies may offer significant opportunities for business consolidation and expansion—as long as the transitions are made in a way that minimizes the risk of failure. This report contains advice to help buyers increase their chance of successfully completing a business acquisition. Among the main recommendations, buyers should strive to:
 - select the right company for them;
 - select a company that has a corporate culture similar to their own;
 - get professional advice;
 - pay a fair price; and
 - choose an effective financing structure.

Context

This report is a follow-up to [*The Coming Wave of Business Transitions in Canada*](#), which was published in September 2017. That study examined the intentions of small and medium-sized enterprise (SME) leaders regarding the sale of their company. Among other things, it showed that 41% of Canadian entrepreneurs intend to sell their business over the next five years without buying another one. Furthermore, it found that these entrepreneurs generally did not take the necessary steps to maximize the value of their company before putting it up for sale.

Drawing from the same spring 2017 survey of more than 2,500 SME leaders that was used in the first report, this follow-up study presents the perspective of buyers (i.e., those looking to acquire another company). What are their characteristics? What are their motivations? What types of businesses are they looking to buy?

Answering these questions is essential for entrepreneurs who want to sell their business. In an environment where many entrepreneurs are looking to sell over the next five years, the information contained in this report will help them better prepare for their upcoming sale.

This report also contains information relevant for buyers. For example, it will help them better understand other business leaders who are in acquisition mode and what they are looking for in a potential acquisition. In addition, they will find advice on how to ensure a successful business acquisition. Finally, this report provides an illustrative case study of an entrepreneur who stands out due to his rigorous approach to acquisitions.

1

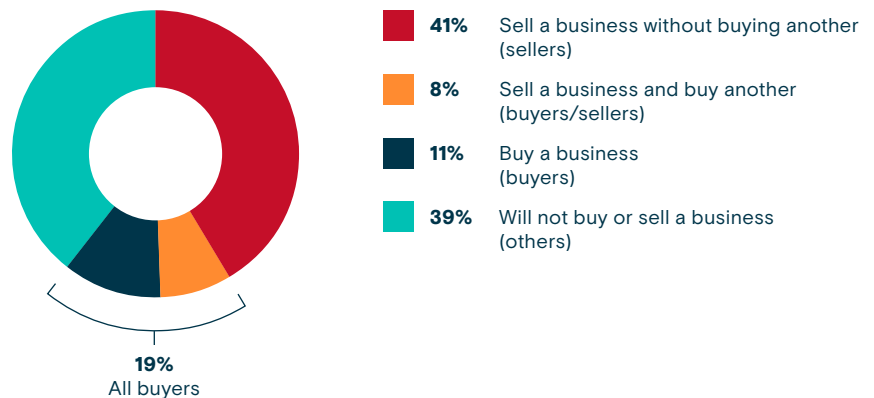
Profile and characteristics of entrepreneurs looking to acquire an SME

Our survey found that 19% of Canadian entrepreneurs intend to acquire a new business within the next five years (Figure 1). Some buyers will make an acquisition while keeping the business they already own (11%), while others will completely divest themselves of their current business (8%).¹

What are buyers' intentions?

Figure 1 – One in five entrepreneurs expects to buy a business within five years

Acquisition and sales intentions of entrepreneurs over the next five years



¹ Buyers: Entrepreneurs who intend to buy a business over the next five years while retaining their current business.
Buyers/sellers: Entrepreneurs who intend to divest their business and purchase another within the next five years.

44%

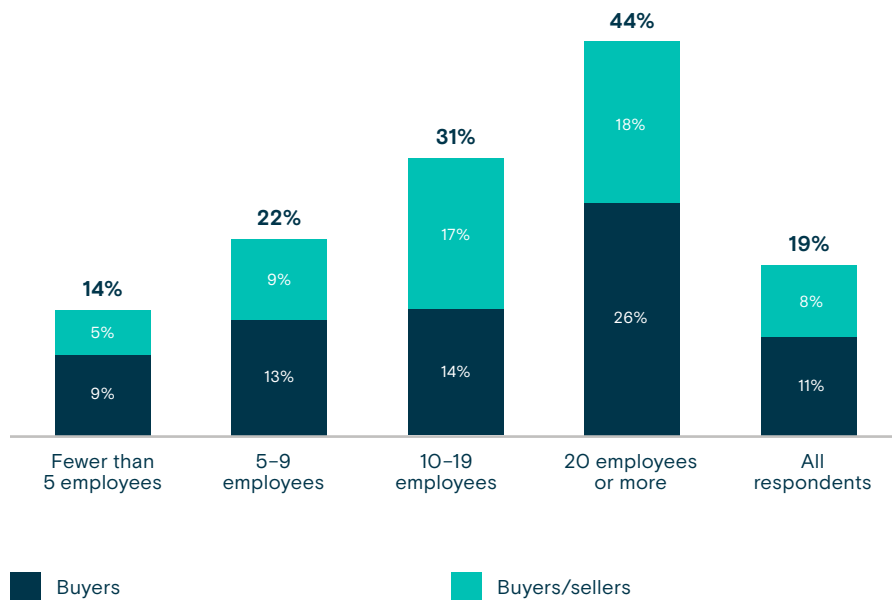
of entrepreneurs with businesses of 20 or more employees plan to buy another company.

Size of buyers' businesses

As a business gets larger, so does its likelihood of acquiring another firm. Among entrepreneurs with businesses of 20 or more employees, 44% plan to buy another company compared with just 14% of those with businesses that have fewer than five employees (Figure 2).

Figure 2 – Owners of larger companies are more likely to make an acquisition

Acquisition intentions of entrepreneurs by size of business



However, it should be noted that while business leaders with 20 or more employees are more likely to consider acquisitions, they represent only 11% of all buyers in the market, while companies with fewer than 10 employees actually account for three-quarters of all future buyers. This simply reflects the fact that businesses with fewer than 10 employees represent a larger share of the SME population.

34%

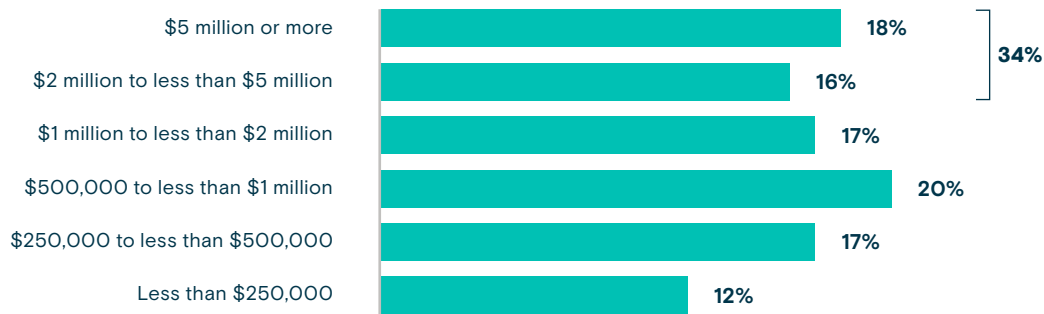
One-third of buyers reported annual sales greater than \$2 million.

Annual sales generated by buyers' businesses

Greater sales mean a higher likelihood of acquiring another firm. One-third of buyers (34%) reported annual sales greater than \$2 million (Figure 3). By comparison, only 25% of all survey respondents achieved this sales figure. This is not surprising, however, as growth through acquisition is a widespread strategy among mature companies that have more resources.

Figure 3 – Owners of businesses that generate more sales are more willing to make an acquisition

Breakdown of buyers by annual sales

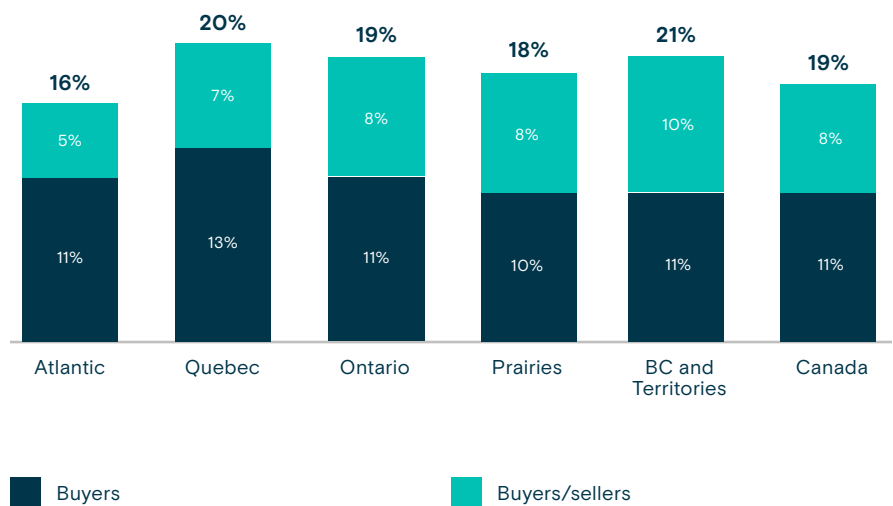


In which region are the buyers located?

Although there are buyers in every region of the country, entrepreneurs in British Columbia and the Territories as well as those in Quebec are slightly more willing to buy another company. Conversely, acquisition intentions are somewhat less pronounced in the Atlantic provinces (Figure 4).

Figure 4 – Acquisition intentions are more prominent in British Columbia and Quebec

Breakdown of buyers by region

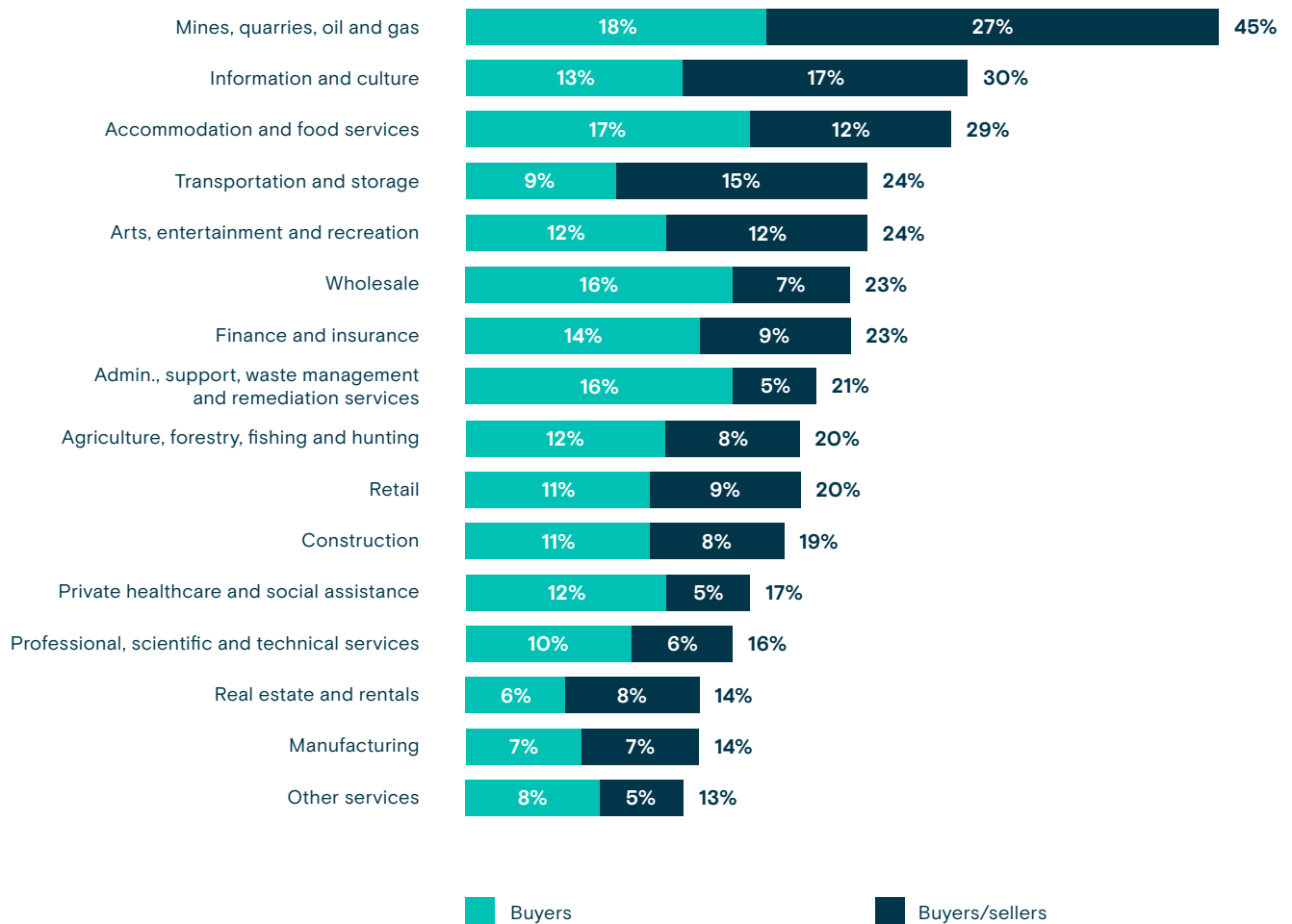


Buyer profile by industry

Buying intentions over the next five years vary by industry. Entrepreneurs in the mining, quarrying, and oil and gas extraction sectors are more active in acquiring businesses, with 45% of those respondents indicating that they intend to buy a business in the next five years. This was followed by respondents in the information and culture sector (30%), with the accommodation and food services sector coming third (Figure 5).

Figure 5 – A greater proportion of buyers are found in the mining, quarrying, and oil and gas sectors

Breakdown of buyers by industry



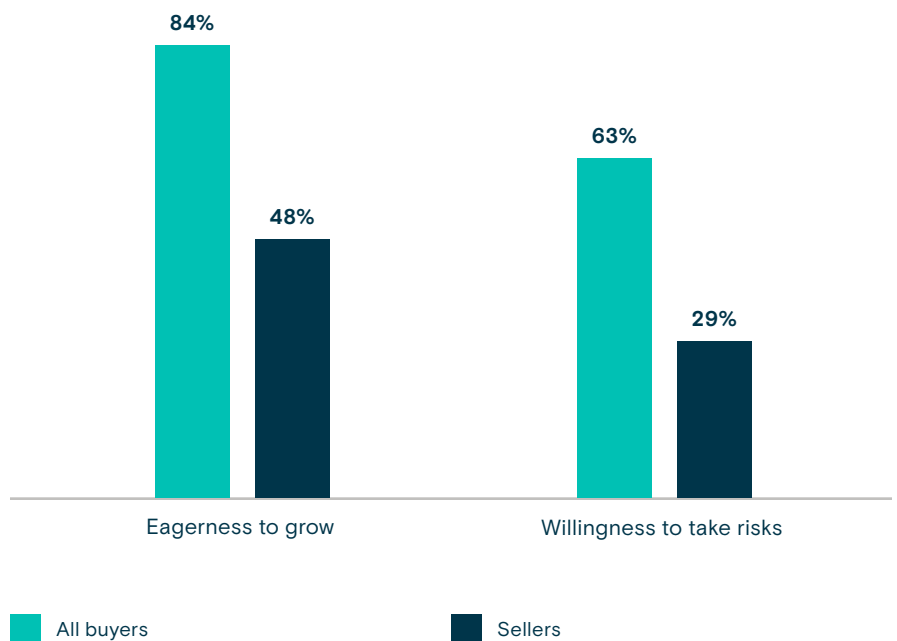
Industries with stronger acquisition intentions are also those in which businesses of 20 or more employees are predominant among the survey respondents.

The buyers' mentality

Unsurprisingly, business leaders looking to buy other companies tend to be in growth mode and are more inclined to take risks (Figure 6). This finding is widespread among buyers, regardless of size or sector. Canadian companies in acquisition mode are undoubtedly among the most dynamic in the country.

Figure 6 – Buyers are among the most dynamic business owners in the country

Propensity to grow and take risks among business buyers and sellers*



* Proportion of respondents who scored seven or more, on a scale from zero to 10 where zero means "Unwilling to grow or to take risks" and 10 means "Very willing to grow or take risks."



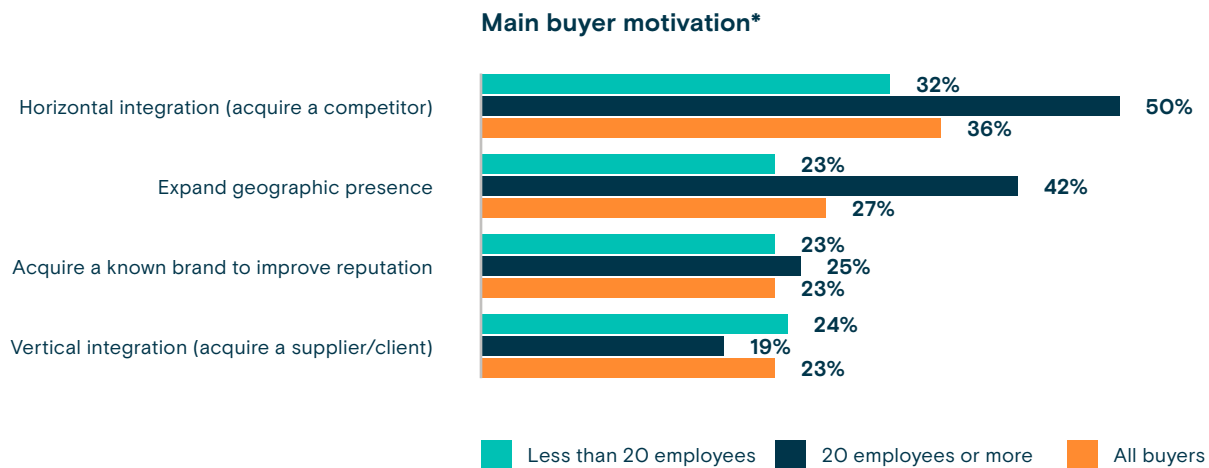
Motivations of buyers and types of businesses sought

What motivates entrepreneurs in acquisition mode? One of the most interesting aspects of this study was the chance to better understand what motivates the decision to buy another business as well as what these entrepreneurs are looking for in a potential acquisition. Are they looking to buy a competitor or expand geographically? How large are the businesses they covet? And do they want a growing and profitable company, or one on the decline that they can turn around?

Buyers' motivations

The survey findings show that the desire to acquire a competitor tops the list of main motivations. This is especially true among buyers with businesses of 20 or more employees (Figure 7).

Figure 7 – Acquiring a competitor is the primary motivation of buyers



* Some buyers mentioned several main motivations, therefore the percentages do not sum up to 100%.

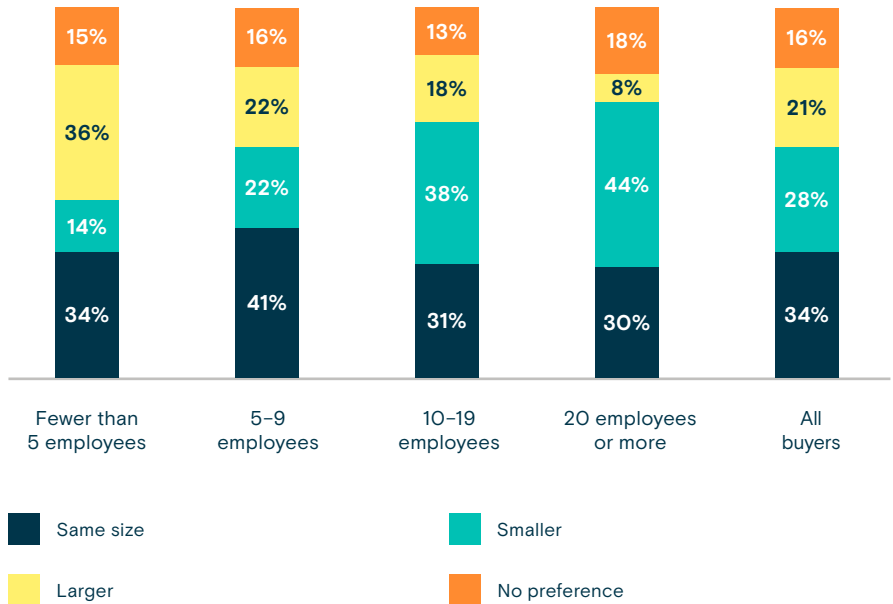
Geographic expansion, whether in another city in Canada or abroad, is the second most important motivation among buyers. In smaller (although still important) proportions, some entrepreneurs want to acquire a company with a recognized brand name to increase the reputation of their own brand. For other respondents, achieving vertical integration (e.g., by buying a supplier or client) is the leading motivation behind their acquisition intention.

Size of sought-after businesses

Buyers are primarily looking for companies of the same size as their own or smaller. This is particularly true among larger SMEs—businesses of 20 employees or more (Figure 8)—that seem to be more cautious. Even buyers with a higher propensity to take risks prefer to acquire businesses of the same size or smaller. This is probably due to the greater challenges that are likely to arise when absorbing a larger business.

Figure 8 – Buyers look for companies of the same size or smaller than their own

Preferred size of acquisition by buyer size



Very few buyers are looking for declining or unprofitable businesses.

Growth and profitability profile of sought-after businesses

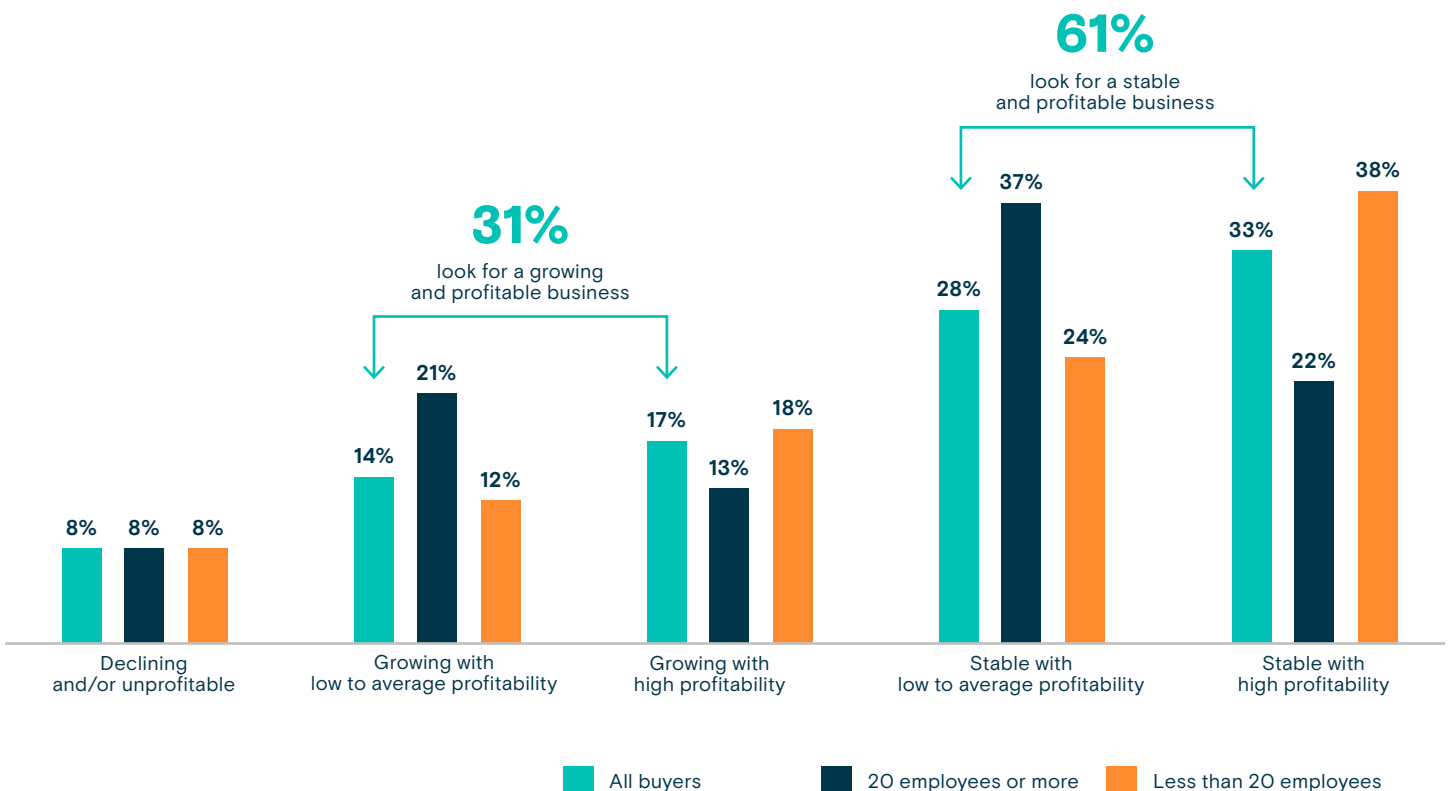
Clearly, more buyers are looking for stable businesses (61%) rather than growing businesses (31%). This may be because it is easier to manage a stable business than a growing one, especially if the growth is strong. This finding applies to all buyers, regardless of their size or willingness to take risks.

Overall, businesses with high profitability are preferred to those with average or modest profits, even if it means paying a premium when making the acquisition. However, this finding does not apply to buyers who lead companies with 20 or more employees. They clearly prefer businesses with profits that are average or lower (Figure 9). These larger SMEs appear less willing to pay a purchase premium but are more willing to invest to improve the efficiency of the acquired business.

Very few buyers (8%), regardless of their size or interest in taking risks, are looking for declining or unprofitable businesses (i.e., companies that need to be turned around before they can start reaping the benefits). A warning for sellers: It is best to ensure the business is strong and profitable before considering a sale; the market for those looking to turn around a struggling business is very limited.

Figure 9 – Buyers prefer stable or growing businesses

Preferred growth and profitability profile for sought-after businesses





“Don’t hesitate to seek expert advice to ensure you pay the right price and close a good deal. Because this is, in many cases, a significant investment, it is worthwhile to surround yourself with professional advisers to limit the risks during the acquisition.”

Benoit Mignacco
Managing Director,
Growth & Transition Capital,
BDC Capital

How to avoid getting burned when buying a business

Benoit Mignacco has nearly 15 years of experience in acquisition, merger and growth financing. He willingly shares his knowledge and expertise to support entrepreneurs.

“An acquisition can be an excellent way to grow your business. After all, you’re buying an established operation with staff, assets and customer relationships. But you have to be careful to buy a company that’s a good fit for your business and makes sense in terms of your strategic plan. You also have to be able to buy it at a price, and with a financing structure, that doesn’t put your personal or business finances at undue risk,” he explains.

First, you have to understand why you want to make an acquisition, develop criteria for what you’re looking for and how much you’re willing to pay. It is essential to stick to these criteria throughout the acquisition process, particularly in “hot” markets with more buyers than sellers, as is the case in many parts of the country.

Here are some tips to keep in mind when buying a business.

→ The right business

Go beyond financial statements to ask lots of questions about the business. Start with the most basic: Why is the current owner selling? Is there a hidden problem or is the industry headed for a cliff? Is the company overly dependent on a few customers or suppliers? Are customers loyal to a charismatic current owner and likely to slip away to competitors when he or she is gone? The folks who do well spend a lot of time searching for companies, studying them and, most of all, do not get overwhelmed by their emotions.

→ The right fit

Make sure the business you're buying has a culture that's compatible with your own. Think of a web-development firm with a free and easy T-shirt and flip-flop style. When it was acquired by a buttoned-down telecom giant, it didn't take long for the acquisition to turn sour. "A common and proven practice is to plan a transition of at least six to nine months with the current owner to ensure the transition is made gradually and smoothly," says Mignacco.

→ The right price

Do your homework on what businesses are selling for in your industry and region. It's important to be disciplined about how much you pay, even if your bankers are willing to lend you more. Overpaying will reduce your financial returns and increase your risk of default. "You shouldn't hesitate to consult experts, such as accountants or lawyers, to make sure you pay the right price," says Mignacco. "They sort of act like the inspectors or appraisers we hire before buying a house. It's a worthwhile investment."

The right advice

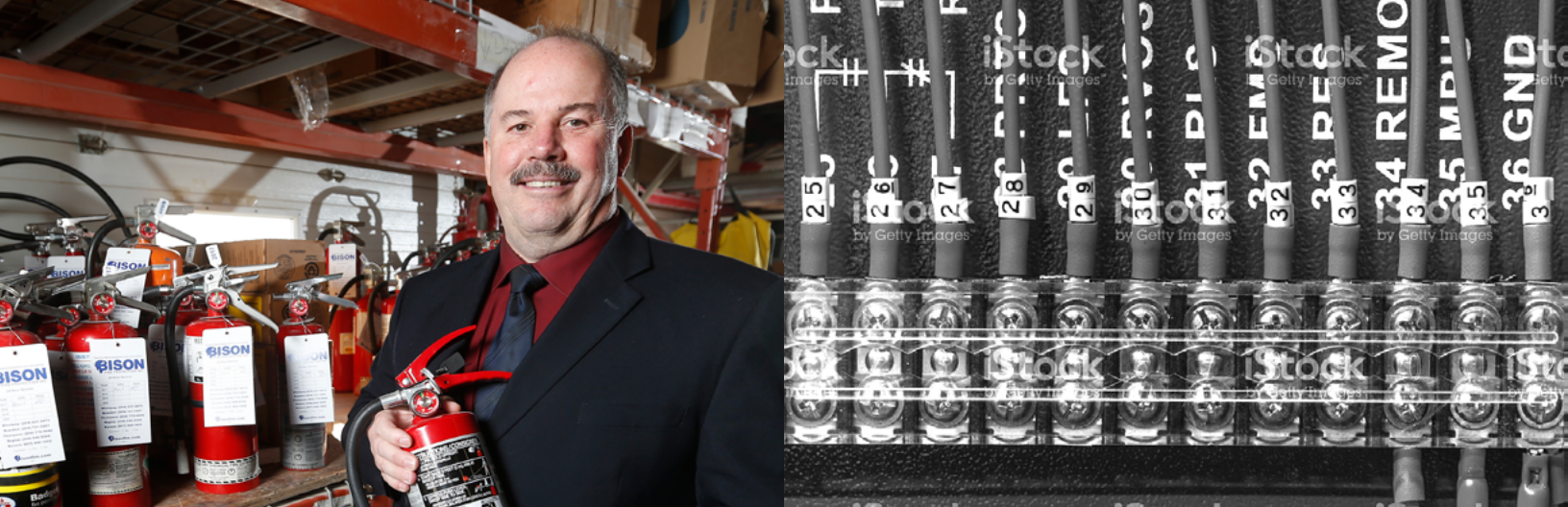
If your internal team is less experienced or busy on other projects, an external team could be brought in for support. They will help you be more objective with due diligence and may prevent you from turning a blind eye to major defects. For example, professionals from audit firms can assist you in the due diligence review of the target company's financial results, accounting procedures, working capital management or contingent tax liabilities. A lawyer specializing in mergers and acquisitions, meanwhile, can advise you on common acquisition agreements, information technology and human resource management practices.

→ The right financing structure

Remember to finance your acquisition in a way that maximizes repayment flexibility. Besides a loan secured on the assets of the company, you should typically seek financing from the existing owner. Vendor financing usually comes with a reasonable interest rate, flexible repayment terms and no personal guarantees. To round out the financing, consider growth and business transition capital because it also features flexible terms and usually requires limited or no personal guarantees. The mix of financing tools that you use can dramatically change the return you realize and what kind of risk you're facing in the company and personally.

→ The right mindset

Patience is a virtue, especially in a hot market. The September 2017 BDC report [*The Coming Wave of Business Transitions in Canada*](#) showed that four out of 10 Canadian small business owners are considering divesting their business over the next five years. This should tip the balance in favour of buyers.



Bison Fire Protection

Lessons learned from a string of acquisitions

This entrepreneur follows a rigorous approach to acquisitions

Rob Read heads a specialized fire protection business that began as a small company in Winnipeg—and now operates six facilities across Manitoba, Saskatchewan and Northwestern Ontario.

Bison Fire Protection owes part of its growth to the three acquisitions made since 2006. Read knows that a single bad acquisition risks compromising his company, which has 85 employees and revenue growth of 25–30% each year. As such, Mr. Read plays detective to find potential targets.

“We go through every step of the due diligence process to ensure the acquisition is viable,” says Read, whose company specializes in selling fire extinguishers, sprinklers and alarm systems. “Believe me, many companies have approached us and, after careful analysis, we declined their offers.”

According to Read, a common problem with the companies he refused to buy is that the owner demands too high a price given the company’s profitability. Often, businesses do not possess assets complementary to Bison such as equipment, inventories and product lines.

Furthering the research on the targeted company

When he is interested in a business, Read analyzes it carefully. He looks at the functional aspects, such as the compatibility of the computer system with that of Bison. But he places particular importance on the competence of managers and other employees. He interviews the owner/seller and speaks with the employees to get an accurate idea of the company’s challenges.

When Read decides to proceed with the acquisition, his team draws up a plan outlining the main stages of integration. From the start, it is essential to communicate with the company’s staff to reassure them about the changes and to gather their suggestions for improving the business.

For Read, one of the primary objectives is to retain the best employees and avoid losing them to competitors or, worse, seeing them start their own business—a phenomenon he has witnessed and says has occurred largely because of poorly organized integration.

“If you don’t do it properly, especially with the staff, it’s a guaranteed disaster,” he says.

Conclusion

A wave of consolidation ahead?

This study examines the business acquisition intentions of entrepreneurs in Canada. It reveals that nearly one in five entrepreneurs intends to acquire a business in the next five years. These intentions increase with the size of the company, reaching 44% among owners of businesses with 20 or more employees.

The acquisition of a competitor tops the list of buyer motivations. In addition, buyers are looking mainly for companies of the same size as their own or smaller, with stable growth and good profitability.

Entrepreneurs who wish to divest their businesses over the next five years will benefit from the findings of this study as it will help them maximize the value of their business. At the same time, buyers will appreciate comparing themselves with their peers.

For the Canadian economy, the coming wave of changes to the management of Canadian companies will provide significant opportunities for business consolidation and expansion, which translates into a better ability to compete in international markets—as long as those transitions are made in a way that minimizes the risk of failure. This report provides buyers with important advice on how to make a successful business acquisition.

Canada will see several business transitions over the next few years. Whether you are buying or selling, it is essential to be well prepared. Buyers need to make rational and informed decisions, the acquisition must be consistent with their strategic plan, and they need to ensure they pay a fair price.

Are you planning to buy a business? For a successful transition, choose BDC

→ Whether you're acquiring an existing business or a competitor's or supplier's business, we offer several long term financing options depending on your circumstances.

→ Benefit from our extensive experience in business acquisition financing. Our professionals will work with you to find the optimal financing structure.

Survey methodology

During March and April 2017, Nielsen conducted a telephone survey to determine the succession and acquisition plans of Canadian companies ranging from one to 499 employees. The results for all respondents were weighted according to the distribution of businesses by province and number of employees.

Do you want to know more on issues impacting small and mid-sized businesses in Canada?

Visit BDC's Analysis and Research webpage.

 [bdc.ca](https://www.bdc.ca)

You will find:

- The monthly *Economic Letter*
- Our Chief Economist's column
- The Oil market update, which is now part of the monthly *Economic Letter*
- The Canadian business productivity benchmarking tool
- And the most recent BDC studies



bdc 
financing.
advising.
smarts.

**For more information,
visit [bdc.ca](https://www.bdc.ca)**

Contact us
T 1-888-463-6232
E info@bdc.ca