The Deal Room Podcast

Episode 142 – Why business acquisition is a killer growth strategy part 1

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Transcript

Joanna: Hi, it's Joanna Oakey here and welcome back to The Deal Room podcast, a podcast proudly brought to you by our commercial legal practice Aspect Legal now today is the first part of the fabulous two part series, we will be talking all about the power of acquisitions for businesses to access exponential growth.

Now this is a topic that I'm really passionate about, because I think it is such an amazing opportunity for businesses to access fast growth as an alternative to what can sometimes be the slow slog of organic growth. And I think it will be remiss of business owners and their management teams not to be thinking about the possibilities of acquisition as part of their growth strategy. So in order to talk about this topic, in this two part series, we have a panel headed by Simon Bedard of Exit Advisory and Nick Wormald of Grow Capital.

So in this part one of the two part series, we begin by diving into why business acquisition is a killer growth strategy. We share the alternative approaches to

achieving growth and the reasons why acquisitions can create an extraordinary opportunity. We look at examples of where the strategy has delivered extraordinary returns, and we reflect on what factors need to be considered in assessing the suitability of acquisition as a growth strategy. And then we also look at funding considerations, the cost of debt versus equity and funding approaches and further examples of stories where acquisitions have played a vital role in achieving substantial growth so buckle in and here we go with part one of our two part series all about why business acquisitions are a killer growth strategy.

Why is business acquisition such a great strategy?

Joanna: Fabulous Simon and Nick, welcome onboard it to the deal room podcast. I'm really excited to have you in this discussion today.

Simon: Thanks for having us Jo.

Nick: Yeah, thanks, Jo.

Joanna: My absolute pleasure. Okay, why don't we kick it off perhaps if you can both just give our listeners a super quick overview of your background? Why are you talking about these topics today? Simon, over to you.

Simon: Great. Well, I'm the CEO and founder of a company called exit advisory group. So we very much focused on business sales and acquisitions. We do a lot of advisory work around that from valuations to helping people understand strategy and how to grow their business. And I think there's a very big difference out there between sort of just growing your top line revenue and actually growing value. So I think that's certainly our passion.

Joanna: Yeah, yeah. Love it. Okay. Wonderful. And Nick, over to you.

Nick: Yeah. Thanks, Joanna. My name is Nick Wormald and I am the Managing Director of grow capital. We're a business finance company. And we, what we do is we help companies SMEs in particular in Australia to grow through the right application business finance. Same as Simon, we're looking at helping to grow businesses. And yes, that's why we are all here.

Joanna: I Love it. Exactly. And I was just about to say that that's the point. That's why we're all here today. I think everyone who listens to this show will probably know all about me and who I am but if you don't know if this is the first time listening to The Deal Room Podcast, well, welcome on board. Welcome. We're excited to have you.

My name is Joanna Oakey, I am the Managing Director of Aspect Legal and we are commercial lawyers and we specialize in driving great deals through business sales and acquisitions. And today we're talking about this concept of acquisition for growth in organizations because we, all three of us are really strong believers in the power of acquisitions for business in terms of giving them access to ways to find exponential growth within their business, most people who listening to this business are involved either in the ownership or the running of the business. And you know, it's a hard game, organic growth can be really hard.

And so today we're talking about an alternative to just doing the grind of organic growth. And really, we're talking here about the opportunity in acquisitions. And one of the things that I like to say about acquisitions is it's the opportunity to add immense value to your business in one single signature. Of course, we all know it's not exactly that easy, but one signature really can make you more. If you do it, well. Then the grind in your business over years and years and years, maybe even decades. So like let's kick into it. And maybe let's start off with just discussing together wide business acquisition is such a good strategy. Simon, what's what's your thoughts on why this is such a good strategy?

The growth concept and the two main ways to grow your business

Simon: Yeah, look, it's so interesting. I think for most business owners out there, if you ask them what they're trying to achieve, it'll be growth, right? Most people's mindsets. growth, to what purpose and what end is often where we start to have some more interesting questions and dialogue with them. But if we just stick with the growth concept for a moment, I mean, really, there are two ways you're going to grow a business, you're either going to build it, or you're going to buy it right? And that's in its most simplistic terms.

If you want to build it, as you said, do the organic route, you know, either option is all going to come down to risk and costs. Ultimately, if people have the time and they want to, you know, grow their business and they're willing to take that time they're willing to take a certain type of risk, organic can work, you know, but then you know, if you want to go out there and hire marketing people and sales people and, and do a lot of spend in various different areas, you know, once again, that carries itself a little risk. The reason I really like this concept of acquisitions is yes, you have to spend the money up front. But that's just the difference between spending it over time on other areas.

You know, as you said before, you can literally get through a deal and massively increase the size of your business, you could get all sorts of complimentary synergies out of a deal like that. And in some cases, where you're actually buying out a competitor, you're actually reducing competition. So there's so many different avenues there. And if you're able to tap that funding and finance side of it, acquisitions can just be a brilliant, brilliant strategy.

Why are there very few businesses using acquisition as a growth strategy?

Joanna: Absolutely. And you know, one of the things that I sort of say, I have this perception that in, in the US, for example, small businesses as a whole are more inclined to look at acquisition as a growth strategy than I feel they are here in Australia. And I feel like there's a lot of there's perhaps a lack of knowledge about that. What do you think of the reasons? You know, why are there very few small businesses using acquisition as a growth strategy?

Simon: Yeah, look, first of all, I agree with your comments about the US. I mean, I

get over there a couple of times a year. And I've got a lot of great friends and colleagues who do similar stuff to us. But at some, I think a lot of it has to do with the maturity of the market over there. It is a lot bigger. I do think that culturally, the US is a little more entrepreneurial than most countries. Yeah. So when you go over there, there's much more of a sort of focus on the deal and the growth and there's a bit of hustle around it. And it's kind of exciting, right. So I just think there's an exposure thing. And I think traditionally, you know, we've been little Ozzie battlers, and people have done these startup companies that they didn't know where they'd go and, you know, having to build an empire out of it. Yeah, I think over time, that'll probably change.

Joanna: Yeah, yeah, I totally agree. I totally agree. Nick, why is it that you think that acquisition is such a killer growth strategy for business?

Nick: Look from what we said we see a lot of clients growing businesses that's what we do we help finance growing businesses and what we've seen of lately is with access to access to the right finance companies are starting to realize that if we tap into a supplier we can purchase a supplier and and on board their business and suddenly we've increased our margins, cut our costs, or we take over a competitor and we now have a large chunk of the market realizing that the purchasing businesses is such as a rocket ship to the end game as compared to a slow moving truck. You know, we see it as Simon was saying we see a lot of this in the States. There are a lot more advanced than what we are with respect to government policies and grants and, and even lending institutions how they fund but we're starting to see that now appear here in Australia and with the right advice it's you can tap into pretty much any type of funding opportunity.

Difference with debt and equity funding

Joanna: Yeah, absolutely. So maybe that leads to the question, why fund rather than bringing investors? What's the difference between debt and equity funding? You know, which is the best to go for, Nick, you probably have a perspective on this one, I'm guessing.

Nick: Yeah, we get asked this question quite a lot. So a lot of transactions that we see actually come to us with people looking for investors, they're looking for equity funding, which is, in essence, they're selling shares in their company for money to grow or to purchase or to improve their business in some form in some form or function, that that can be very expensive going forward. When they have a company in the multiples the value is, as increased by 10, 50 to 100 times Then that shareholders equity has now increased by 10, 50 to 100 times it's quite a can be quite expensive.

Joanna: Do you know what that is? You are so spot on. And we have a deal going at the moment with the business, who during startup decided to do a bit of a deal where rather than go and get funding, he gave equity to a number of people who were throwing in some cash and also some services. Well, that business has just grown phenomenally. And he now has a multi million dollar issue to get rid of these shareholders and with equity comes control issues quite often as well. And so we're having to grapple with some of these control issues right now. For something that, you know, was his baby all along, but he just thought it seemed like a good idea at

the time to tell you what would have cost him you know, maybe 100 grand in Funding initially is now costing him millions and millions. And so that just sort of rands home. I guess the issue, what's your thoughts on it all? Simon?

Simon: Yeah. Look, I think Nick really made the point. Well, I mean, equity is always more expensive than debt, always, especially if you're on a growth trajectory. You know, and I think when you couple that with the fact that we're in a record period for low interest rates, yes, don't get me wrong. We've been through COVID.

We've had, you know, other funding challenges, which I'm sure Nick and his team would be able to assist with but, you know, put aside some sort of temporary issues there. You know, we've got low interest rates, we've got a government trying to stimulate growth and stimulate more business. So yeah, look, it's just, it is overall a good environment to be looking at debt as opposed to giving away shares. And let's be honest, as you sort of pointed with your example, Jo, once the share is gone it is gone right? It cost you significantly to get it back. And that issue of control is a massive one and, you know, I think all of us here have dealt with family businesses in the past. And I don't know about your experience but a lot of my clients went into business for themselves because they didn't want to answer to anyone else.

Setting real examples

Joanna: Yeah, that's so true. Yeah. And they're not good at answering other people that's the other thing, like they're just not good at it. Yes, I agree. Yeah, it's really interesting. Okay. All right. So what I think we should go here is maybe let's talk, let's make this real. Let's talk about some examples we've seen in the market, because I think that can really help our listeners connect to what we're actually saying, in a real sense. So maybe Simon over to you what some examples have you seen of this really kick off well?

Simon: Yeah, look before I perhaps give some specific, you know, industry sector example stuff like that. I mean, the way we generally see things is there's a number of acquisitions of types if you like, out in the market, you know, different sort of styles of player with a lot of aggregators out there who like private equity guys, right? You know, they see an opportunity in a particular sector they buy, maybe one company is a bit of a beachhead or foothold into that sector.

And then they run around buying up the competition, right, and basically do a bit of a roll up with the view that there is an eventual exit. And that might be going IPO, it might be doing another trade sale to a much larger organization. And they're very interesting. We can touch on some examples around that. Of course, other things you see are just straight trade players, right? You have a business that's a manufacturer, they know there's a guy down the road or another state over who does similar stuff, and perhaps they're competing already. So one buys the other and that's they're far more common. I would say and, and yeah, and then, of course, you're saying other types of acquisitions where it's more of a complimentary play.

And like if I was to give you an example of that, let's just say for a moment you manufacture tables, and down the road, there's a guy who manufactures chairs. You don't buy and sell from each other and you don't compete with each other. But Geez, there's some synergy there, right? And so one of those companies acquiring the other

would make a lot of sense. That wouldn't just, you know, grow the overall revenue pie, but they'd get a lot of synergy cut costs, do a whole bunch of other things there as well. So, there's probably just, I guess, kick it off as this sort of three different types of segments that we see out there in the market at the moment.

Simon: Yeah, absolutely. Great. Okay. And so Nick, of using many examples in any of those sort of types of segments that Simon brilliantly set out for us.

Nick: Absolutely. See them every day. One of our clients Currently, the manufacturer of frames for high end residential, and, and small commercial. So yeah, wall frames, floor frames, and roof truss frames. They have suppliers that make those frames up outside of the factory. So there's only one thing that they do and they have supplies that provide them with I guess, then the end result of what they're going to sell them. That's what this applies to. So the idea was to, hey, if we buy our suppliers, we actually purchase those companies and with all of the equipment that that comes with, we can tack on their margin directly onto our margin, and we reduce costs. We also synergize as we have this, this big product we can sell directly from our warehouse. So there's a huge increase in productivity, decreasing costs and increasing profit in that business through those purchases.

Joanna: I love that as an example, because one of the things that you're talking about Simon is about private equity or PE in the in the aggregator space, you know, but one of the things that I think is really important to point out is that each of those sectors that you're talking about the aggregation or the, you know, the buying other strategic, complementary businesses, whatever, it's all also, this is available to smaller businesses as well. Isn't it?

So Nick, you've sort of, you've given us a great example of how that can play out well for smaller businesses as well to take control of the supply chain, and then, you know, bring them higher margin, but also, you know, potentially access to a wider client base, you know, because they coming in at a different point of the funnel, and certainly, you know, we act for a number of aggregators, but I'm just thinking one of our aggregators in particular, what they do is and they started out quite small, and they use traditional funding sources, you know, like the sort of funding that you can you guys can organize Nick and what they did was they took that funding and they started buying small, small medical practices and what they're able to do out of that because they were starting small.

They were sort of taking a bite size, giving it a go, adding another one in slowly and so we moved them through and we probably Up to, you know, maybe eight or nine or 10 acquisitions for them now, but now they've got something really solid and out of that they can turn into something in a few years time that maybe they can look at an IPO for. And then rather than paying a multiple of two or three for really small practice, they can now look at, you know, a multiple of 13. If they can IPO or if they do a trade sale, if it's a five times multiple now they're paying, you know, what's interest rate at the moment, Nick, for businesses that you're dealing with in your area? I love that I liked the laugh. Haha

Nick: Interest rates range from 3 to 50.

Joanna: Yeah, well, let's not take the 50 let's say though, we were closer to the

under...

Nick: If you're buying a business and your bank ready, then you're going to be looking in the sort of, you know, 5, 3 to 7's. If you're going to have private money, i.e. non banking money, then you'd be looking sort of early to mid teens.

Joanna: Yeah. But let's say even early to mid teens, right? You're paying that for an acquisition on the basis of two or three times multiple, but within a few years time or five years time even you're able to roll it up for a trade sale and get a multiple of eight times. That's far more than the entire I mean, you know, massively more than the interest you're paying, which you know, why I think it's such a good strategy for business.

Nick: Absolutely. And look, what happens is what we see because we see a lot of these aggregations, and they're constantly coming across the desk. What we see is that the initial funding to get that business connected is expensive. But once there's a track record, 12-18 months two years down the road, we can back that out with a major bank and significantly reduce the cost of capital.

Joanna: Strategy of it as well, right, the strategy of the approach. And so what about you, Simon? What else have you seen in this space that sort of has some rock your socks? You know, it's been a really good way of playing this.

Simon: Oh, look, we've seen deals in all of the categories that I talked about. Most recently, we've had a number of deals in that aggregator space that we've seen also in the medical and allied sort of health areas. So there were some movements around in physio, there's been medical practices, dental, a whole bunch of things in that space.

But we're seeing some other interesting ones too, that right through from consulting services in particular sectors, logistics right through to even a really detailed AI strategy for a company that was basically a word identified about 117 different competitors globally, and they really wanted to team up and see what they could do to go on a climb. So yeah, really, really interesting stuff happening there. Of course, we do say a lot.

The typical family business has been around for 3040 years. They know the other family quite well, they compete, but you know, it's perhaps a let's call it a respectful competition. And you know what some of those deals often just come around to buy them actually lifting the phone and going, I'm done. You want to buy it? Because you will want this more than anyone else, right? And of course, then they actually need to get their good advice, somebody to help run the transaction, somebody to fund it and somebody to manage the legals and make sure everyone's getting what they buy.

Joanna: Yeah, yeah.

Nick: Yeah we see that? The children, once they take over, the parents move up and the kids come in? And they merge them together? Yeah

Simon: Yeah. It was a sort of different outlook on it all right? You know the next generation will see things differently? And technology's changed all has what's

changed and you know.

Nick: Yeah.

Joanna: Yeah. You're right.

Joanna: Well, that's it for part one of our two part series, all about why business acquisition is a killer growth strategy. I hope you found today's podcast useful and informative. And if you'd like more information about the topic, then just head to the show notes, which you can see in the podcast player that you are using at the moment to listen to this podcast or head over to our website at thedealroompodcast.com now there at that website, you'll be able to download a transcript of this episode if you'd like to read it in more detail, if you're a detail oriented person but at our website, we will also have details of how you can book in to our webinar talking all about nailing the strategy of growth through acquisition.

We have that webinar running really soon after the launch of this podcast episode. And so it might be that when you're listening to this podcast episode, you miss out on that webinar live. But don't worry, just head to the show notes and we'll give you details of how you can access that recording of the webinar if you'd like to catch up on the event and learn a bit about the strategy of growing through acquisition. Now back to our show notes and our website we have linked through to the fabulous Simon Bedard at Exit Advisory and we'll also link straight through Nick Wormald at Grow Capital. And on our website, you'll also find details of how to contact our lawyers at Aspect Legal If you or your clients would like to discuss any legal aspects of sales or acquisitions. We've got a number of great services that help businesses prepare for exit offer acquisition and certainly we have a lot of experience in helping guide businesses through this whole topic of acquisition for growth, so don't hesitate to book in a free initial discussion with our legal Eagles at Aspect Legal if you'd like to discuss how we might be able to assist you in your acquisition or your exit. Well, that's it for today's episode.

Please don't forget to come back and listen to part two, where we finalize our discussion about this great topic all about acquisition as a killer growth strategy. In part two, we look at the importance of understanding a broader scope of the market. When dealing with acquisitions, we talk about how buyers can clearly understand their funding requirements, both for the acquisition and for the future requirements of the business. And we also share a whole heap of actionable tips and real case studies as examples of businesses who have very successfully implemented this as a strategy for growth in their business. So we look forward to joining you in part two But until then, thanks for listening in. You've been listening to Joanna archy and the deal room podcast, a podcast proudly brought to you by commercial legal practice Aspect Legal. See you next time.