

The Psychology of Exits

Transaction Roadblocks
and Intangible Negative
Value Drivers

Introduction

- We sell businesses, why are we talking about psychology?
- What are intangible negative value drivers?
- Even if we cared, what can we do about them?
- I believe this is a bigger part of our business than most of us appreciate

The Biggest Negative Value Driver?

- What's the most significant negative value driver?
- It's one that prevents the transaction from closing
- Because then the entire result is zero
- Or worse - a negative number

What Percentage Close?

- What percentage of M&A transactions close?
- After an M&A Advisor has been engaged?
- In my experience, it's fewer than half
- I heard a speaker from a large multi-national M&A Advisory firm say:
- Only 8% end up closing

What Causes M&A Failures?

- We don't have hard data
- But either of those percentages is dismal
- For both the Seller and the M&A Advisor
- Why do “saleable” businesses fail to sell?
- Is the fault most often with the Buyers?
- Or the Sellers?
- Or the M&A advisors?

Causes of Exit Failures

- Certainly some individual transactions fail due to the Buyer
- But when a saleable company fails to sell,
- I believe it's usually because the Seller or M&A Advisor failed
- (There are almost always other Buyers)

What Actually Goes Wrong?

- So how often is the failure to sell due to:
- The selling company?
- Or the M&A Advisor?

Sometimes it's the M&A Advisor

- There is no question that some M&A Advisors have a much higher close rate
- And that a lot of the failures are due to the people in our industry
- But in this presentation, I'd like to focus on the most frequent source of failures
- The Sellers

Two Main Reasons Sellers Fail

- There are two reasons the Sellers are the most likely cause of an M&A failure:
- The business becomes un-saleable
- The Seller's psychology
- Which do you think is the most frequent?
- I think Seller psychology is the most likely

Do Sellers Really Kill Deals?

- Most Sellers won't understand that they are the most likely reason
- Their companies might fail to be sold
- Almost all prospective Sellers believe they are ready and willing to sell
- Otherwise, why would they have hired an advisor?

Exit Strategy Alignment

- In my experience, the most common intangible negative value driver
- Is lack of alignment on the exit strategy
- It's surprising how often the key stakeholders don't really agree on the goal
- And end up disagreeing when presented with a serious offer to be acquired

Valuation Expectations

- The two key elements in the exit strategy:
 1. **Timing, and**
 2. **Valuation**
- It continues to amaze me how often a Seller
- Who has engaged an M&A Advisor,
- Gets all the way to an offer while still having
- An unrealistic value expectation

Seller Psychology

- None of us are very good at looking at ourselves objectively
- If you don't believe that, just ask your wife or husband.....
- Sellers are just people
- They are no more perfect than the rest of us

It Feels Like I am Selling my Child

- Many business owners, especially founders,
- Built a paternal, or maternal, attachment to their businesses,
- For many the entire concept seems “wrong”
- And in some cases they may not be able to explain why
- It’s often an “attachment” issue

My Business is Me

- “I spend more time with my business than my spouse”
- “This is why I get out of bed in the morning”
- “This is my reason for being”
- “And why people like me”
- “What else would I do?”
- “What else can I do?”

I am Still Having Fun

- Or “I am too young to sell”
- Most often this has more to do with unmet life ambitions
- And sometimes the Seller’s relationship to their fathers (especially in family businesses)
- These can require some psychological ‘heavy lifting’ to work through during the exit

Fear and Greed

- Up until the written offer, the Sellers fret about getting the price they want
- Surprisingly often, when they actually see that someone is willing to offer that much,
- They have a new perception of the value,
- And ‘fall back in love’ with their business
- Or decide they want to hold out for more

I am the Smartest Guy in the Room

- One of the fastest ways for a Seller to defeat themselves is to get stuck on
- Being the smartest guy in the room
- This is especially common with founders
- Who often are the smartest guys in the room
- Until the Buyers show up
- And then they have trouble accepting advice

Approach Avoidance

- Term often applied to airplane pilot trainees
- Who have a phobia about landing
- Sometimes circle until the fuel runs out
- I have seen the same psychology in sellers
- Who just can't seem to put pen to paper
- To sign the binding agreement

Cloaked Decision Makers

- Sometimes the person who looks like the decision maker
- Isn't really
- It can often be a spouse, or mentor
- And they are also just human
- And will often effectively veto a good sale
- Based on their psychological imperfections

I Believe Most Do Want to Sell

- But it's their imperfect human psychology that defeat them
- It is a common characteristic many of us share
- A large part of the M&A Advisors' job is to help the seller work through the psychology
- I often feel we should charge for counseling

The Two Important Sales

- In the M&A Advisory business, there are two important sales we need to close
 1. **When the Seller agrees to engage our firm**
 2. **When the Seller agrees to accept an offer**
- I believe each of these decisions is as affected as much by
- Seller psychology as by money

OK, What Can We Do About It?

- If you accept that psychology is a big part of completing a successful exit
- What can we do to improve our outcomes?
- A few of my M&A Advisor friends just keep looking for the prospects that are perfect
- (Their children aren't going to good schools)
- I think the real question is how can we help?

How Can We Help Our Clients?

- The most important point about the impact of psychology on exit transactions is
- “How can we best help our clients?”
- First, we have to accept that for owner operated businesses, psychology is
- A big part of our business
- Possibly as big as the financials

Why the Sellers Need This Help

- Seller's usually haven't experienced an exit before
- It is a huge life transition
- And usually the biggest financial transaction of their lives
- It's not surprising they need help with the
- Non-financial aspects of the transition

Building Psychology Into Our Model

- Once we accept that Seller psychology is an important aspect of our business,
- I believe we have to work it into our models
- Make it a component of our prospecting, qualifying and closing processes
- Expand our skills, our teams or our affiliations to deliver a full service