William Blair

williamblair.com

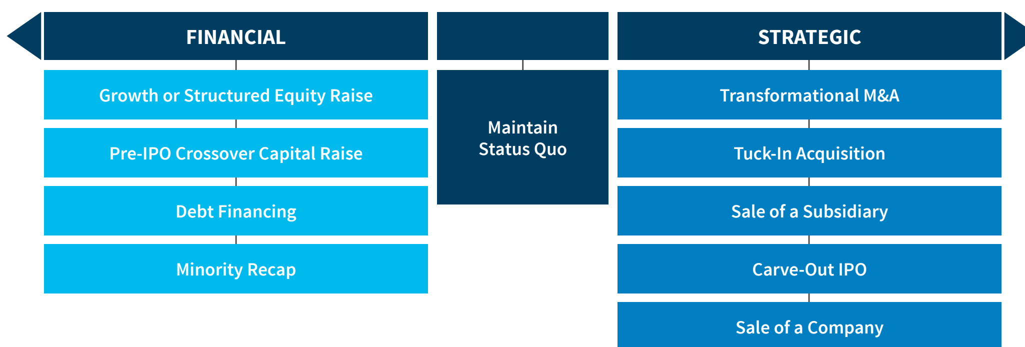
How Business Owners Can Evaluate Financial and Strategic Alternatives to Maximize Value

There are myriad ways that a private company leader can chart a new course for their enterprise. And when considering the available alternatives—which can be classified as either strategic or financial—they should consider three important questions:

1. How will it impact value creation?
2. How will it impact growth?
3. What are the risks and timing associated with execution?

To answer these questions, executives need a firm grasp of the available alternatives paired with a strong understanding of their company's current position. The following article lays out the benefits and considerations of exploring these alternatives.

Potential Strategic Alternatives



A Premier Advisor for Nearly Nine Decades

Since 1935, William Blair has guided owners of closely held businesses and their trusted advisors through monumental decisions. Our relationship-driven approach empowers owners to maximize the value of their businesses—and turn that capital into an enduring legacy. We invite you to contact us to discuss the ways we support and advise business owners and help our clients capitalize on the tremendous opportunities available to them today.

Financial Alternatives

There are several alternatives to consider for companies hoping to raise capital or recapitalize and restructure the company's existing capital structure.

1. Growth or Structured Equity Raise

Minority growth investment from a partner that shares a compatible vision to reinvest the proceeds and help accelerate growth

Benefits	Considerations
Growth equity raises attract investors with appetites for risk who can provide operational support and industry expertise to accelerate growth. Capital can be raised via a bespoke solutions (such as a debt-like equity security or equity with downside protection) to meet company objectives, and that money raised can be flexibly deployed.	New investors often require board representation and existing owners will have their ownership diluted. Additionally, added governance associated with the raise can be a burden to the company.

2. Pre-IPO Crossover Capital Raise

Equity raised from institutional investors a year or two before a company pursues a traditional IPO

Benefits	Considerations
A crossover establishes a baseline value for the public offering and cements long-term public shareholders who are typically hands off.	An IPO is typically required within 12-24 months, and once public, the company will face increased pressure to meet Wall Street expectations and quarterly targets.

3. Private Debt Financing

Broad spectrum of debt financing sources that provide a range of structures to fulfill a company's objectives

Benefits	Considerations
This eliminates equity dilution unless warrants or convertible instruments are included; the interest costs are tax deductible and typically a lower cost of capital compared with an equity raise.	With increased interest costs comes reduced cash flow and restrictive covenants/collateral requirements. Additionally, balance sheet flexibility can be limited depending on future performance and leverage levels.

4. Minority Recapitalization

Capital raised through equity or debt financing with the proceeds going to liquidate existing shareholders

Benefits	Considerations
Recapitalizations create immediate value without the need to sell shares or issue regular dividend payments while providing the opportunity to refinance existing debt at lower interest rates.	Existing debt restrictions and covenants might stand in the way and can be coupled with increased leverage levels, potentially limiting future financial flexibility.

Strategic Alternatives

Companies explore strategic M&A options after assessing current operational objectives and identifying the most viable value-creating path for shareholders.

1. Transformational Merger or Acquisition

Acquire scaled business or engage in a merger-of-equal transaction

Benefits	Considerations
A merger or acquisition of this size moves the needle and can drive meaningful revenue and cost synergies while addressing challenges associated with lack of scale as well as improving the cost of and access to capital.	There is significant operational risk related to integrating consolidated service/product lines. And depending on balance sheet flexibility, the company will likely have to meaningfully increase leverage or use equity financing to pay up for the right asset.

2. Tuck-in Acquisition

Acquisition of a smaller company that can be integrated into the acquirer's platform

Benefits	Considerations
A tuck-in can create time- and market-sensitive opportunities to acquire assets at accretive multiples with low risk compared with transformational M&A while still growing market share or adding a new resource capability.	This is unlikely to "move the needle" for value creation in the short term, and a dedicated in-house corporate development team is usually required to effectively execute a tuck-in strategy to scale over time.

3. Sale of a Subsidiary

Sale of a smaller business segment or non-core service/product line to a strategic buyer or financial sponsor

Benefits	Considerations
Generates cash that can be redeployed across the business, fund future acquisitions, pay down existing debt, or return capital to shareholders via a dividend while possibly helping simplify a company's strategy and narrow its focus to fulfill longer-term objectives.	The sale has potential for a loss of synergies and management distraction stemming from preparing to shed a non-core asset. Depending on the transaction's structure, the sale could also result in significant tax liability.

4. Carve-out IPO

Parent company sells shares (typically no more than 20%) of a subsidiary through an initial public offering

Benefits	Considerations
In addition to generating cash, the parent company retains trading value and control of the new company.	Going public and separating the business brings added costs and disclosures—and the parent company's ownership might limit trading activity.

5. Sale of Company

Full liquidation of the company's equity interests to a strategic buyer or financial sponsor

Benefits	Considerations
Potential for quicker liquidity and crystallized premium in the near-term compared against the company's long-term value while transferring business execution risk to the buyer.	The process can be disruptive to management and the risk of a leak or failed process may create unwanted operational challenges such as employee/customer uncertainty, aggressive competitor reaction, etc.

How to Execute on the Status Quo

Of course, a company can simply pass on these alternatives and focus on executing its current strategic plan through reinvesting operating cash flows to drive organic growth, strengthening the margin profile, and improving efficiencies across the enterprise's processes and systems. That doesn't preclude a more transformational move in the future and waiting might allow more value to be captured over time.

But there's market and execution risk associated with any business plan—and not achieving organic growth objectives might disadvantage a company to competitors that are scaling more rapidly. Further, a particular market outlook from a multiples perspective, or the appropriate moment to act, might not last.

With numerous financial and strategic alternatives, business leaders have a lot to think about. While operational strategies are company-agnostic, one constant is the need to regularly evaluate the benefits and considerations of different paths to maximize value creation.

William Blair Founder-Owned Business Advisory Team:

Andrew Hansen
+1 312 364 5439
ahansen@williamblair.com

Sam Longenecker
+1 312 364 5237
slongenecker@williamblair.com

February 2023

William Blair" is a trade name for William Blair & Company, L.L.C., William Blair Investment Management, LLC and William Blair International, Ltd. William Blair & Company, L.L.C. and William Blair Investment Management, LLC are each a Delaware company and regulated by the Securities and Exchange Commission. William Blair & Company, L.L.C. is also regulated by The Financial Industry Regulatory Authority and other principal exchanges. William Blair International, Ltd is authorized and regulated by the Financial Conduct Authority ("FCA") in the United Kingdom. William Blair only offers products and services where it is permitted to do so. Some of these products and services are only offered to persons or institutions situated in the United States and are not offered to persons or institutions outside the United States. This material has been approved for distribution in the United Kingdom by William Blair International, Ltd. Regulated by the Financial Conduct Authority (FCA), and is directed only at, and is only made available to, persons falling within COB 3.5 and 3.6 of the FCA Handbook (being "Eligible Counterparties" and Professional Clients). This Document is not to be distributed or passed on at any "Retail Clients." No persons other than persons to whom this document is directed should rely on it or its contents or use it as the basis to make an investment decision.