Developing Your Company's Acquisition Criteria: A Guide

After nearly a decade of austerity and investor conservatism the climate has changed and M&A deals are decidedly on the rise. Why? Today's large companies are seeing the strategic imperatives to do deals, they have the cash make deals, and they can borrow additional cash at record low rates—a perfect storm when it comes to dealmaking. Many companies are also sitting on large cash reserves, which are gradually eroding in our current low-interest rate climate, so there's motivation to utilize that money.

If M&A is part of your company's growth strategy it is critical to develop a comprehensive acquisition criteria checklist that will enable you to define both the ideal and essential characteristics of the businesses you are targeting. A well-deveolped acquisition criteria checklist allows you to define carefully enough what you are looking for so that your search efforts are well-directed, but not so narrowly that you overlook qualified targets. The process of developing an acquisition checklist can also reaffirm your company's goals and bring your overall strategic plan more clearly into focus. Use the list at right to define your company's acquisition criteria.

What Are You Looking For?

- A unique product with low to medium technology processes?
- A proprietary product?
- A leadership position with a market niche?
- Gross margins of ?%
- A closely-held private company entering ownership transition?
- Corporate divestitures of non-core business units?

What Industry Characteristics Are Desirable?

- Manufacturing (service and/or distribution elements only as support for primary manufacturing process)?
- Non-cyclical?
- Significant barriers to entry?
- Highly fragmented with potential for consolidation or growth?

What Industries Are You Interested In?

- Life Sciences?
- High-tech?
- Software?
- Medical?

What Areas Do You Have No Interest In?

- Automobile?
- Food Service?
- Commercial Real Estate?

Define Parameters

- Are you looking for a start-up business?
- What kind of sales volume are you looking for?
- Is geography a concern?
- What size of investment are you willing to make?
- What will be the structure of the deal? Controlling ownership?
- What will be your ongoing involvement?
- What will be the long-term focus for the acquired company?

What Key Strengths are Desirable?

- Channels of distribution—use current or develop new?
- What are the manufacturing capabilities?
- How are the products differentiated?
- What is the customer base? Do you plan to reinforce long-standing relationships with current customers or develop new ones?
- Sales force? Current or develop new?
- Brand recognition? Is it currently strong or does it need improving?

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M&A can be a powerful growth strategy for your company; it should be approached both thoughtfully and intentionally. Nuances and risks abound, as do the rewards if done correctly.

Sample Acquisition Criteria for Acme Corporation

I. Key Desirable Strengths

Channels of Distribution— Interest Level: High

Acme currently has a strong presence in the office products channel in both retail and contract. For example, Staples, Office Max, Boise, Corporate Express, United Stationers, SP Richards and Office Depot.

Acme is targeting alternative channels, such as mass market (Target, Wal-Mart); specialty retail (Crate and Barrel, Bed Bath and Beyond) and retail pharmaceuticals (Walgreen's, CVS).

There is a preference to acquire a company that has a strong presence in one or more alternate channels as a means to increase revenue and profit.

Manufacturing Capabilities— Interest Level: Moderate

A target that works in "metal bending," particularly if it were a similar or compatible product offering would enhance the acquisition because consolidation could accelerate savings and utilize existing assets. However, manufacturing is not a primary driver in the deciding factor. Strong global sourcing capabilities or current manufacturing capabilities in China would also be considered a plus.

Product Differentiation— Interest Level: High

Desirable product offerings can be divided into two categories. The first is direct competing products from an existing competitor. The second are companies that are not competitors; however, they offer products related to money handling, security, or related to banking use or applications. These companies may be suppliers to Acme, for example.

Customer Base— Interest Level: High

Acquisitions that bring new customers to Acme have significant value. This includes clients in traditional channels or alternate channels.

Sales Force— Interest Level: Low to Moderate

Acme currently sells primarily through independent sales representatives. An acquisition that also uses independent representatives would, therefore, be a relatively simple and preferable transition. However, a company that has a direct sales force could also provide an alternate or new primary way to market if that sales group is managed reasonably well and, therefore, would also be considered.

Brand Recognition— Interest Level: Variable

Name brand recognition would be a definite plus. However, unless the brand drives clear market leverage across our existing line, we do not have a strong desire to pay the premium goodwill often associated with a recognized consumer brand.

II. Financial Criteria

Target Revenue

The ideal target company will have a revenue between $10 million and $40 million. Companies under $10 million would certainly be considered, and we would like to be made aware of available companies over $40 million, but they would be less likely candidates in the near term.

Multiples

The target multiple we would be willing to pay for the "right" acquisition is between 5 and 7 times earnings.

III. General Profile

Acme would consider the following profiles:

- **Manufacturers**
- **Importers**
- **Suppliers**
- **Competitors**

These companies should have their headquarters in North America, with preference in the United States. However, if the U.S. company also has distribution outside of the U.S., this could be considered desirable.

A good acquisition criteria checklist allows you to define carefully enough what you are looking for so that your search efforts are well-directed, but not so narrowly that you overlook qualified targets.