




Mergers & Acquisitions in the Electrical Contracting Market

Robert Kirkpatrick
Broadside Advisors



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Agenda

- Overview and history of the market
- M&A drivers
- What buyers are looking for
- What is EBITDA?
- Anatomy of a Transaction




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Overview and History of the Market

- Strategics have always been interested in M&A
 - Growth strategy
 - Expansion
 - Acquiring new capabilities
- Private equity has a long history with facility services investments
 - Focus has been primarily on HVAC
 - Recently there's been more activity around electrical contractors

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Overview and History of the Market

- Deal volume is increasing
- Sharp decrease in 2H 2022 due to interest rates rising
- Valuation multiples in some segments had been at/near historical highs prior to 2H 2022
- Multiples have settled at or above historical averages



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M&A Drivers

- Large amounts of “dry powder” for investing
- Success in adjacent markets
- Increase in focus on alternative energy/EV charging/etc.
- NFPA standards

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What are buyers looking for?

- Size
 - Buyers will be looking for a platform company or an add-on
 - Platforms (first company) should be \$5 million of EBITDA or more
 - Add-ons, including by strategics, can be smaller
 - Still need to be substantial compared to the current business
 - Valuation difference can be huge
 - However, don't chase revenue/EBITDA with low margin or risky work

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What are buyers looking for?

- Business mix – best to worst
 - Maintenance agreements – gold standard
 - Service work off those maintenance agreements
 - General service work
 - Project work, especially with repeat customers and on mission-critical facilities
 - Purely new construction/bid work

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What are buyers looking for?

- Low customer concentration
 - Ideally no single customer above 10% of revenue
 - Might get away with have one at 15-20% in special situations
 - Higher concentration raises the risk of more earnouts (if the transaction closes at all)

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What are buyers looking for?

- Low "YOU" concentration
 - Good company or good job?
 - Management bench strength
 - Diverse major customer relationships

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What are buyers looking for?

- Reviewed or audited financials
 - If you are considering selling, start now
 - Will speed up due diligence process
 - Will want 3 years minimum, ideally 5+

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What are buyers looking for?

- Systems and processes
 - Accounting system
 - Work Order Management
 - HR
 - Order to Cash

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What are buyers looking for?

- How do buyers view union companies?
- Strategics
 - If they are union, will consider both union and non-union
 - If non-union, likely not to consider union companies
- Private Equity
 - If this is their first/platform investment, tend to favor non-union
 - Add-on investments will be based on the platform company

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What are buyers looking for?

- What are some buyers hesitant to buy union companies?
 - Misconceptions around unions, especially in this industry
 - Withdrawal liabilities/underfunded pension plans

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What is EBITDA?

- Earnings Before Interest, Taxes, Depreciation and Amortization
 - A *proxy* for cash flow
 - Generally simpler to calculate – operating income + depreciation + amortization
 - Not as useful when there is high capital expenses or large working capital changes
 - Has become the standard measure of valuation

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What is EBITDA?

- Adjusted EBITDA
 - Owner addbacks
 - Excess compensation
 - Personal vehicles
 - Family in the business
 - One time expenses
 - Legal
 - Accounting, CRM, etc. systems
 - Occasionally, you can get away with adjusting for a bad job
 - Any synergies with the combined business you can claim

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Anatomy of a Transaction

- Two types of transactions
 - Stock deal
 - Asset deal
 - Each as distinct tax and legal implications



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Anatomy of a Transaction

- Stock deal (Equity Purchase)
 - Buyer acquires the seller's shares
 - Generally, the seller pays capital gains rates
 - Buyer does not get to amortize goodwill
 - Often maintains licenses, certifications since the corporate entity didn't change

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Anatomy of a Transaction – Stock Deal



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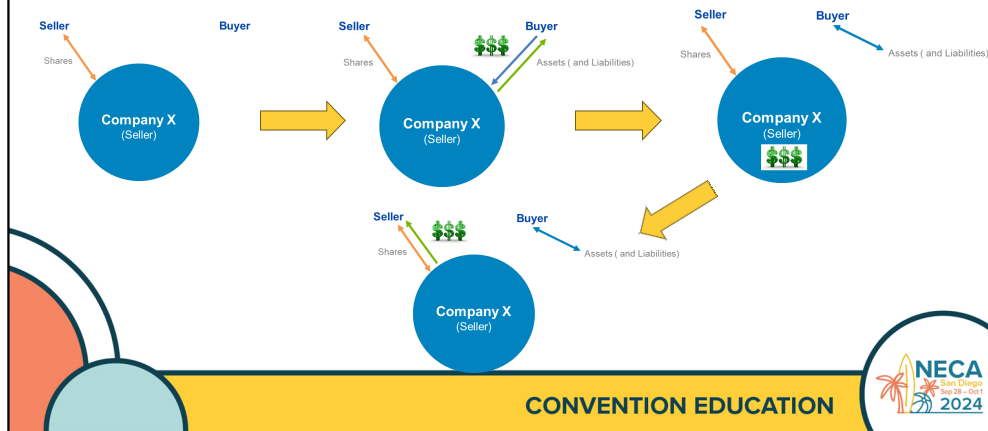
Anatomy of a Transaction

- Asset deal
 - Buyer buys the assets of the company, assumes certain liabilities
 - Contracts
 - Has to hire the employees
 - Generally, the seller pays corporate income tax rates
 - Buyer gets to amortize goodwill
 - Key difference – buyer is paying the company, not the owners
 - Unless the company is a pass-through entity, another taxable event may occur when money goes out to the owners
 - Legal entity remains as a shell corporation

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Anatomy of a Transaction – Asset Deal



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Anatomy of a Transaction

- Offer letter components
 - Enterprise value – the “valuation”
 - Usually given on a “debt free, cash free” basis
 - Structure of the consideration – cash, rollover equity, etc.
 - Working capital requirement
 - Amount left behind in Current Assets less Current Liabilities
 - Earnouts
 - Holdback
 - Timeframe
 - Process to close

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Anatomy of a Transaction

- What does debt-free, cash-free mean?
 - Debt has to be paid off, either before closing or as part of the closing payments
 - New owners will want clean titles, no encumbrances, and their banks will want the old debt removed
 - Bank loans, lines of credit, vehicle loans, and capital leases are all included as debt (operating leases are not included)

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Anatomy of a Transaction

- Working capital requirement
 - Amount necessary to “grease the skids” of financing day-to-day operations
 - May be specifically defined in the offer letter, but simply Current Assets (except cash) minus Current Liabilities (less debt being paid off)
 - Required amount usually based on some historical lookback
 - Excess/deficit will adjust the purchase price

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Anatomy of a Transaction

- What does debt-free, cash-free mean? (part 2)
 - Cash free means that the owner is free to take *excess* cash out of the business prior to close (or depending on the buyer, can get paid for the excess cash)
- The concept is that the business has earned the cash, paid taxes on it or will after it's distributed, and since the buyer is paying for future earnings, current cash belongs to the seller.

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Anatomy of a Transaction

- Considering selling?
 - Get everything in order – address the issues in What are Buyers Looking For
 - Make sure you can produce quickly items that will come up in diligence
 - Get your team together
 - Accounting
 - Legal
 - M&A Advisor

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