



HOW AN INDEPENDENT MARKET STUDY IMPROVES PRIVATE EQUITY EXITS

By Russell Kellner, Peter Czerepak, and Lorenna Buck

A MARKET STUDY DELIVERS AN independent, objective assessment to potential buyers of the market, the competitive position, and the growth prospects of a divestiture candidate. It also helps private equity firms prep portfolio companies and their senior management for transactions, in many cases revealing possible strategic moves that could make a company more desirable.

Done correctly, a market study tells a rich, fact-based story that greatly simplifies the work of the buy-side due diligence team and presents a strong case for making the deal.

Why Do You Need an Independent Market Study?

We saw this education process emerge as a major success factor in the sale of an industrial goods supplier and reseller. The company sat in the middle of a long supply chain, one that began with manufacturers and extended through the supplier to resellers to the end customer.

A rigorous market study by BCG detailed and illuminated how the company achieved strong performance during the most recent five-year period, in part by aligning its portfolio to the highest-growth product categories.

A closer look at the market through a survey and one-on-one interviews revealed that the company enjoyed the highest recognition rate among resellers and led suppliers in the number of clicks on a leading aggregator platform. These gains gave it a digital advantage over its competitors. Bolstering that advantage further was the finding that the company was positioned well in the market with regard to factors that typically drive resellers to switch suppliers, such as product quality, product availability, and shipping times.

BCG's independent market study estimated potential growth opportunities for the company if it expanded its digital presence, expanded its core offerings, and took advantage of acquisition opportunities in both its existing lines and adjacent markets, among other strategic choices.

How an Independent Market Study Positions You for the Best Deals



ENABLES

- Correct messaging that targets investors' objectives
- Fact-based storyline that describes the firm, its history, and its future prospects



PREVENTS

- Deal-killing surprises uncovered during due diligence
- Investors' arguments for a discounted purchase price



SIGNALS

- A quality offering, approach, and business to potential buyers
- Worthiness of premium price and capital investment
- Attractiveness for private equity investment in an increasingly competitive marketplace

Source: BCG analysis.

With its competitive advantages and the benefits and potential opportunities available for further gains, the company was sold successfully to another private equity firm.

Avoiding Deal Killers and Discounts

A well-executed market study anticipates issues that could either kill a deal or impose a discount on the final price.

CONSUMER GOODS SUPPLIER

In a market study of a consumer goods supplier, BCG found that the company's sector was highly susceptible to economic cycles. The market experienced a 10% drop in CAGR during the Great Recession and higher-priced items in this category fared the worst during all downturns.

But the study also discovered that since the crisis, the company had dramatically changed its business mix and was far less likely to be weakened during the next downturn. The owners wanted to avoid the issue of the company's performance during the recession, but BCG encouraged them to address it up front and own the messaging.

Anticipating and addressing issues such as the impact of market events ultimately

strengthened the case for the deal rather than sowing doubt.

INDUSTRIAL GOODS MANUFACTURER

Consider another company, a maker of industrial products used in retail and industrial complexes. This company obtained much of its sales from retailers, a sector challenged by new competitive forces such as online shopping and the entry of Amazon.com into the market.

BCG conducted an independent market study that found the company secured only a small portion of its revenues from department and variety stores, the sector hit most dramatically by e-commerce. By contrast, our analysis found that a comparatively large portion of revenues came from the expanding industrial market, such as factories and fulfillment centers.

Further, the study found that the company's many well-known brands left it well-positioned to make new bundled offerings. It also had a proven track record of driving value from acquisitions, increasing revenues, and improving margins.

And the study validated a wide variety of growth opportunities, including those in aftermarket maintenance, installation services, and the addition of sensors to create smart

products—as well as by acquiring companies and products in new geographies.

BCG's independent market study found that the company held up well during recessions, in part because its products are required for safety, legal, or operational reasons and must be replaced as soon as they are broken.

Understanding the Stakeholders

One of the most critical steps in a market study is to survey stakeholders across the value chain—suppliers, customers, employees, competitors—to determine how the company is perceived by each of these key groups.

DISTRIBUTOR

In another recent independent market study, conducted for a product distributor, BCG found that customers held very favorable views of the company based not just on price and product quality but on such differentiating factors as expertise, inventory reliability, delivery speed, and customer service.

The company was a preferred partner for suppliers, outperforming its competitors across all distributor selection criteria, as well as the most well recognized and used. Customers also saw it as best in class across such criteria as product and market expertise and breadth of skills.

These factors positioned the company well to capitalize on customer switching, BCG's independent market study concluded. Interviews with suppliers revealed that they were rationalizing their use of distributors, consolidating with fewer partners, and putting in place formalized distributor management programs. The company was uniquely well positioned to benefit from these trends.

At the same time, suppliers continued to favor specialty distributors like this one over Amazon, preferring their expertise, specialized pricing, and customized products. The company earned high marks for these very offerings.

BCG's independent market study also revealed several areas of possible process improvement, including reviewing the pricing structure, better aligning sales force incentives, pursuing greater automation and standardization, and consolidating the vendor base.

Choosing the Right Partner

In general, market studies apply buy-side due diligence logic to preparing the divestiture candidate and its management team, enabling the seller to confidently pursue the highest price for the asset. The choice of a partner should take the following factors into account:

- **Industry Expertise.** The right partner will bring deep and relevant expertise in the industry, ensuring an efficient process and important context setting in developing the study.
- **Functional Expertise.** To the extent that you wish to frame underwritable value-creation opportunities, it is imperative to bring depth to the study's estimates and assertions. Depending on your unique situation, this might include such matters as pricing, operations, marketing, sales, and IT.
- **An Understanding of Buyer Dynamics.** It is important to view the company through the eyes of potential buyers in order to understand which issues—strategic or financial—will excite them the most and will need to be presented in the greatest detail.
- **Objectivity and Brand Strength.** To maximize the usefulness of an independent market study, you must ensure that buyers will view it as unbiased, analytically sound, and delivered by a firm known for high standards.

The independent market studies that BCG conducts leverage our deep industry expertise, ensuring that in every facet—market profile, customer profile, competitor and supplier analysis—we produce insights that are unbiased rather than deal-driven.

Our experience also ensures that the study focuses on opportunities for future value creation as much as on the present. And it signals quality to potential acquirers.

INCREASINGLY, AS PRIVATE equity funds demand a more complete understanding of their prospective targets, an independent market study that meets these stan-

dards will be indispensable to firms looking to sell. In most cases, the cost of a market study is more than offset by the gains of encouraging more buyers, shortening due diligence periods, and increasing the likelihood that the seller will obtain a higher multiple.

About the Authors

Russell Kellner is a partner and managing director in the Boston office of Boston Consulting Group. You may contact him by email at kellner.russell@bcg.com

Peter Czerepak is a partner and managing director in the firm's Boston office. You may contact him by email at czerepak.peter@bcg.com.

Lorenna Buck is a principal in BCG's Boston office. You may contact her by email at buck.lorenna@bcg.com.

Boston Consulting Group (BCG) is a global management consulting firm and the world's leading advisor on business strategy. We partner with clients from the private, public, and not-for-profit sectors in all regions to identify their highest-value opportunities, address their most critical challenges, and transform their enterprises. Our customized approach combines deep insight into the dynamics of companies and markets with close collaboration at all levels of the client organization. This ensures that our clients achieve sustainable competitive advantage, build more capable organizations, and secure lasting results. Founded in 1963, BCG is a private company with offices in more than 90 cities in 50 countries. For more information, please visit bcg.com.

© Boston Consulting Group 2019. All rights reserved. 12/18 Rev 1/19

For information or permission to reprint, please contact BCG at permissions@bcg.com. To find the latest BCG content and register to receive e-alerts on this topic or others, please visit bcg.com. Follow Boston Consulting Group on Facebook and Twitter.