
How Independent Sponsors Get Great Economics.

This report will show you how you can improve your Independent Sponsor economics and what we are seeing in the marketplace.

INTRODUCTION

Independent Sponsors have rapidly become an “asset class” in the middle market M&A world. The last five- six years have seen an explosion of Independent Sponsors in the marketplace. What is interesting though is that Independent Sponsor economics are not “cut and dry”. The economics an Independent Sponsor gets for their deal may appear to be “standard”, but they are anything but. Frisch Capital Partners knows from decades of experience and hundreds of proposals that Independent Sponsor economics vary widely and that there are certain criteria make all the difference in the world.

The following paper gives specifics for Independent Sponsors to help them achieve great economics on their next deal.

While there are a great number of nuances to being a successful independent sponsor, there are three main considerations in every deal that drive great economics for the Independent Sponsor.

The first is the Independent Sponsor themselves.

Who are they? Where do they come from? What value are they bringing to the table?

The second is the deal itself.

What multiple are you buying it at? What industry is it in? What is your thesis around it?

And Finally, the third is the element of time and competition.

How do you leverage your exclusivity under the LOI? How do you bring in competition to get the best deal – quickly.

We will focus on each of these now.



FIRST - The Independent Sponsor Themselves

An Independent Sponsor has to be able to “talk the talk” and prove that they can “walk the walk”. It involves having a “thesis” that is appealing to capital partners, which can be clearly articulated. Their thesis must provide focus, vision, and most importantly, how their particular “know – how” will increase the bottom line. Often Independent Sponsors consist of a team of 2 or 3 members each providing different strengths. This provides for a good “bench” because capital providers appreciate depth. A good exception to this we see is when the Independent Sponsor is a C-Suite executive who has the opportunity to buy a company and step in and run it as a CEO.

Obviously, Independent Sponsors have to work hard, very hard. They are the “tip of the spear” on a transaction. If they want good economics they have to KNOW their deal and the industry space extraordinarily well. The more an Independent Sponsor can demonstrate how their experience and expertise are relevant and add value to the deal the better the economics can become. In addition to having expertise, and almost as important, is how do they interact with capital providers. Independent Sponsors have to be flexible, personable, coachable and have staying power. Capital providers realize they are going to be together for years to come and they have to be able to work together in the “trenches” with their Independent Sponsor. Likeability, reasonability, and proficiency actually matter. A good Independent Sponsor is the foundation to great economics.

The deal dynamics are what are going to capture the capital partner’s attention, but it will be the “you” dynamics that keep them there, and get you the best deal. This must not be forgotten as we now go ahead and talk about the deal aspects.

SECOND – The Deal Itself

The deal itself is critical. How much are you paying? What industry is it in? Who are the competitors? Is there customer concentration? What are the financial trends (margins, EBITDA, etc)? For an Independent Sponsor to get great economics it’s helpful to have a deal that appeals to many capital providers. This may seem obvious, but it’s not – and the number one most appealing aspect is the cost.

Price matters. What you pay for the company in terms of a multiple of EBITDA (or EBITDA minus CapEx) is one of the MOST important details to getting multiple capital



sources interested in your deal. This also means that there is more room in the capital structure and returns to cut the Independent Sponsor in on the economics, leading therefore to getting greater economics due to increased interest and increased competition.

Along those same lines, one of the more harmful characterizations of Independent Sponsors is the fact that they will often bid the highest price for a company. Capital providers are smart. No, let me repeat that. Capital providers are VERY smart. They know the marketplace. They are in there every day. They know the appropriate prices and they also realize many Independent Sponsors bid the highest prices in order to win the deal. Winning the deal at the highest price appeals to virtually no one, except the Independent Sponsor. Even if you are the best Independent Sponsor in terms of your background, bidding too much for a company doesn't allow for great economics. You may get the deal done, but there is no room for you to get cut in and certainly not great economics for you.

Due Diligence. Do your homework! You are the tip of the "spear" as an Independent Sponsor. You must be able to articulate the value of the transaction, explain the historical numbers and margins. Speak to the potential upside and most definitely be able to identify and provide mitigants to the various risks. You must know the competition and the exit multiples of similar companies who have gone before and you must know the drivers of the EBITDA. Finally, you must understand the company better than it understands itself. Why? Because you are going to not just convince, but to show, capital providers that YOU are able to take the company to the next level.

THIRD - TIME & COMPETITION

The third and final aspect to achieving great Independent Sponsor economics regards time and competition. Once an Independent Sponsor has a transaction under LOI, it is typical that they will only have 90 days to complete the transaction. Here at Frisch Capital, we always advise our Independent Sponsors to get an automatic extension for another 30 days for a total of 120 days. Regardless of whether or not an Independent Sponsor gets an extension, the moment the LOI is signed, the "clock is ticking". Wasting time is costly. So, let's discuss how an Independent Sponsor often wastes time.

- They think they have to do a lot more due diligence before starting the process of talking to us.



- a. They wait for more information from the company before getting started.
 - b. They don't know how to prioritize the key pieces of information.
- Worst of all, they get stuck talking to one, two or even five capital sources.
 - Those numbers just don't work. These Independent Sponsors get bogged down in answering questions that lead to "dead ends" and worse, burn time.
 - Interest is not to be confused with commitment.
 - The clock is ticking...remember. So many times Independent Sponsors get caught being offered lousy economics- if any at all – and feel they have to take them.
 - Here at Frisch Capital we manage the entire capital raise process for our clients allowing them to more efficiently focus on due diligence, managing the seller, pipeline of acquisitions, and all the other things pulling at your time. We take a "targeted-wide" approach when taking a deal to the market place and go out to hundreds of firms on every deal. Our capital database has thousands of names of capital providers. While we go out to a large number, every group we show it to is hand selected by our team for a specific reason. In other words, we go to capital providers that are interested in the space, want to work with Independent Sponsors and can move quickly. **We bring in proposals, great partners and have the capital partners compete for your business.**
 - **Competition is critical for getting great Independent Sponsor economics.**
 - Without competition, it is very difficult to get **great** Independent Sponsor economics. Competition holds a capital provider's "feet to the fire" and allows us to negotiate a better deal for our clients.
 - However, competition does more than just provide great economics for our Independent Sponsor. Competition also gives you choice and allows you to pick your partner. And arguably the most important thing is with competition and getting multiple proposals, we are able to provide backup bids for the transaction thereby allowing a greater "certainty of closing" within the timeframe of the LOI.



In closing, Frisch Capital Partners is able to continually get great Independent Sponsor economics for our clients because we focus like a “laser” on each of the three areas discussed:

1. Who the Independent Sponsor is and their value add to the transaction.
2. The deal itself. What is the Independent Sponsor buying? Is it attractive?
3. How quickly can we bring the deal to the marketplace and through competition receive multiple proposals?

If you want to learn more about what we are seeing in the marketplace or how we can help, please schedule a call today.