What's the deal?

Diary of an MBO

Livingstone Guarantee recently advised the management team at Uninterruptible Power Supplies on a multi-million pound buy-out of the business. In an exclusive article for **Business 550**, Gordon Blair and Nigel Morgan from the firm give a month by month account of the deal process

There is no such thing as a cosy MBO - it is merely a recipe for conflict: management always seeks the lowest purchase price possible while the existing shareholders are naturally anxious to obtain the highest sums of cash available.

Normally corporate finance advisers are appointed by both "sides" to undertake negotiations and complete a deal that is acceptable to all parties at the same time minimising the requirement for vendors and purchasers to face each other across the negotiating table too often.

The sale of Uninterruptible Power Supplies (UPS) to its management team was an MBO that was an exception to the rule. Corporate finance boutique Livingstone Guarantee was asked to advise the shareholders on the sale. Some 80% of the shares were held by the Vendor who jointly founded the company; the remaining 20% was split between four members (and co-founders alongside the Vendor) of the management team. As the team's interests moved from being vendors to purchasers, it became apparent that the best solution for all parties was an MBO. This is the diary of the deal:

February

The Vendor made his first approach following a personal recommendation from a business colleague who had had dealings with us in the past. He asked us to assist him to realise the shareholder value within the company he had founded approximately nine years earlier.

March/April

We put together a team - Partner Gordon Blair; Director Nigel Morgan; and Deal Leader, Graham Carberry - to investigate the business. We found a company highly respected within the secure power industry that supplies and installs its own range of proprietary hardware under the PowerWAVE brand to in excess of 2,500 individual uninterruptible power supply installations across the UK.

May

Following initial discussions with the Vendor we began a marketing process. Having evaluated all his options, we suggested that he should consider a private equity backed MBO - a VIMBO. We felt this would enable him to secure his shareholder value while offering remaining management the chance to release some equity value today, whilst also reinvesting some capital to enable them to take a more significant stake in the ongoing company.

This was music to the Vendor's ears. He had never believed a deal of this type was an option - he expected us to undertake a trade sale on his behalf. He was generous to admit to us that we had alerted him to opportunities that he did not know existed for an owner. manager in his situation.

June

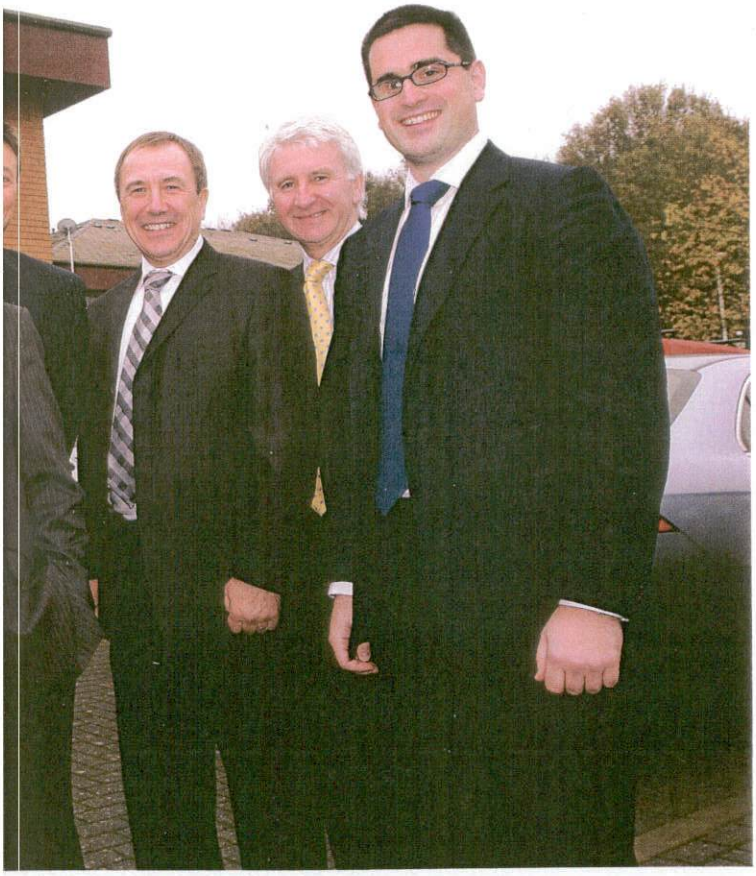
Meetings with the management team in their executive roles, and as shareholders, revealed a clear appetite for a management buy out. Furthermore all demonstrated they had the potential to take the business forward although this was a totally unfamiliar process for them. Part of our role was obviously going to be to get them through this process.

Oct 2006

It was a natural development that David Bond, the recently appointed CEO who enabled the Vendor to become executive chairman, should lead the buy out.

Generally our assessment of the management and the dynamics of the business gave us confidence that a deal could be agreed that would satisfy all shareholders interests. It was operating in an interesting and exciting market, with a proven track record, and had a solid business model which would be attractive to funders.

To confirm these views we undertook a financial modelling exercise designed to evaluate whether a satisfactory deal could be funded, whilst also achieving a suitable price for



selling shareholders - and a viable equity stake for ongoing management.

We then helped them to prepare a detailed presentation to four private equity investors who we knew, from our knowledge of the business and the management team, would be interested.

July

Presentations were made. The team demonstrated a fine working knowledge of the business and the sector and while the majority shareholder was still working almost full time, they were able to demonstrate their capability to run the business independently of him.

Feed back was extremely positive. They all felt the team had the appetite for a buy-out so we asked them to submit initial offers, clearly highlighting the equity stake available.

This was critical to the success of the deal because the headline price had to satisfy the Vendor's expectations while the equity percentage for ongoing management needed to be sufficiently attractive for them to reinvest in the deal. Furthermore the remaining percentage and the achievement of the business plan was structured to enable the private equity house to make the returns they required. We received a range of offers and undertook negotiations with all of them to make sure we achieved the optimum deal.

Following a review of revised offers, and having clarified key terms and conditions, a meeting was arranged with all shareholders to agree the best way forward. Barclays Ventures offered the most attractive deal to the Vendor and to the management team for whom one of the dynamics of the deal was the payment of cash for their shares to enable them to reinvest in the new business opportunity with an enlarged equity percentage.

August

We agreed detailed heads of terms with Barclays Ventures and a detailed time table for completion.

September

Initial due diligence was undertaken on the business, the market place and the management by reporting accountants, commercial due diligence advisers, and because two freehold properties were part of the transaction, it was necessary to use property and environmental due diligence advisers as well. Ongoing discussions with the funders about management, deal and business issues allowed a number of points raised to be clarified and the overall timetable kept on track.

Conscious that the management team was still required to run the business day-to-day and ensure there were no problems that would affect and impact on the funding structure (let alone the headline deal) we worked with them to ensure their acquisition and banking agreements were reached. Barclays Ventures had approached several banking partners, but the best overall package was offered by HSBC Leveraged Finance.

All was progressing smoothly, then only days before completion, following the release of the property due diligence report, an indemnity was called for because of a property issue that indicated that there would be no valid insurance against which to claim in the event of a fire. Negotiations to rectify the problem were carried out post deal.

October 19, 2am

The completion took place at the lawyers of Barclays Ventures in the City of London. Almost 20 people sat round the table. The meeting began at 5.30 p.m. The circa £15m deal was finalised at 2am the following morning - and substantial quantities of champagne had been consumed half an hour later!

The completion immediately put David Bond and the management team in a position to further enhance the already excellent reputation of the company and increase its market share, taking advantage of the inertia in larger UPS suppliers and the problems faced by smaller distributors and suppliers who are unable to provide a customer service led approach. 550