MidMarketCapital,Inc.

Gentlemen, So How Much Do You Want for Your Software Company

By Dave Kauppi CBI, President MidMarket Capital

I will never forget this scene. We were in the board room of a one billion market cap NYSE traded company representing our client, a small software company. We thought we were going to meet with the general manager and his team from the $100 million division that was going to utilize our client's product. In walks the Executive Vice President and after some brief introductions he says, "Gentlemen, so how much do you want for your company?'

I looked over at our clients and watched as the color drained from their faces. They looked back at me as if to say, O.K., Dave, this would be where you step in. Taking the hint, I started down the path of suggesting that we wanted to understand the synergies between the two companies. I was quickly taken off my course with the EVP saying, "I appreciate what you are trying to do, but how much do you want for your business?"

It was almost lunchtime and I knew that they had ordered sandwiches for a working lunch. I requested that we huddle separately and that we could reconvene after lunch. After they left us, I said to our clients, I know exactly what is going on here. This guy is trying to quickly determine whether these entrepreneurs are realistic in their expectations and will be worth continuing discussions or whether they should catch the next plane back to Chicago.

This situation was complicated by the fact that we had other interested buyers, but were early in the process and had no other offers thus far. This buyer was the number one strategic buyer. In other words, they are the company that can create the most economic value in the three years following the acquisition. That is impacted by such factors as how close the new product meshes with their existing product suite, how many installed accounts they have, the number of salesmen, etc. Finally, we were going to be seeking a transaction value that would not be supported by any traditional valuation models. We were seeking an aggressive strategic value.

We generally like the buyer to offer first, but the EVP was making that very difficult. The worst thing that could happen to us is that we say we want $5 million and he immediately responds, we'll take it! It is almost impossible to negotiate up from there. So our challenge was to come up with a number and deal structure that did not short change our owners while not scaring off the buyers.

We had done our research and found that our client's product was a logical add-on to their existing product that was installed in approximately 1100 accounts. They were

102 S Quincy Street Hinsdale, IL 60521
PH: 630-325-0123 • FAX: 630-325-9879 • Mobile: 630-215-3994
davekauppi@midmarkcap.com www.midmarkcap.com

getting pressure from a well funded venture backed company that had a similar product and also had designs of displacing the buyer's core offering. This new product category was getting a lot of attention from other major competitors as well.

Emboldened by this information and bolstered with our analysis of factors such as:

Time to Market
Window of Opportunity
Development Cost
Brand Name Pricing Leverage (a big company can charge 25%-50% more for the identical product)
Potential Customer Base Defection

We made our pitch, discussed these points, and presented our value and deal structure request. Then we held our breath. The EVP, a tough but charismatic New Zealander looked at us and said, "That's outrageous, but not bloody outrageous. Let's talk." Well we caught the late flight back to Chicago that night with a commitment for a qualified letter of intent within the next three business days.

We still had a lot of work left, but the groundwork was set for productive negotiations, due diligence and a completed sale.

David Kauppi is a Merger and Acquisition Advisor with Mid Market Capital, Inc. MMC is a private investment banking business brokerage firm specializing in providing corporate finance and intermediary services to entrepreneurs and middle market corporate clients in high tech and a variety of industries. Dave began his high tech Merger and Acquisition practice after a twenty-year career within the information technology industry. His varied background includes positions in hardware (Storage Technology Corporation), IT Services (IBM's Service Bureau Corp. and Comdisco Disaster Recovery), Software (Metaphor Computer Systems), computer leasing (Bell Atlantic Systems Leasing), datacom (Paradyne Corp.), and Internet (DigitalCars.com). The firm counsels clients in the areas of merger and acquisition and divestitures, succession planning, valuations, corporate growth and turnarounds. Dave is a Certified Business Intermediary (CBI), a licensed business broker, and a member of IBBA (International Business Brokers Association) and the MBBI (Midwest Business Brokers and Intermediaries). For more information or a free consultation please contact Dave Kauppi at (630) 325-0123, email davekauppi@midmarkcap.com or visit our Web page http://www.midmarkcap.com