## New Media Age – 24th May 2007
## [Page 1 of 2]



The market is ripe for digital businesses looking to sell up, but that doesn't mean you can just wait for buyers to come to you. **Sean Hargrave** looks at what investors want

# On the market

New media firms wanting to realise the value of the past few years' hard work are in a fortunate position. There has never been a better time to consider selling, and 2007 is shaping up as a record year for digital investment.

With so much money available for new media acquisitions, it's a seller's market where company owners have a mouth-watering selection of possible exit strategies. The big names that rose to prominence at the start of the decade are now reinvesting to keep up to date, hence Google's $1.6bn bid for DoubleClick following last year's purchase of YouTube.

Traditional players are buying a share of the digital market, such as News International buying MySpace and WPP's string of recent acquisitions of companies like VideoEgg and LiveWorld (NMA 17.05.07). At the same time, venture capital and private equity money is flowing into digital in the UK as advertising and marketing budgets reflect changing consumer habits.

In short, if you own a successful new media business – or at least one that's believed to have the potential to be successful – there has never been a better time to dip your toes in the water to see what options there may be, according to Jon Hustler, partner at Clearwater Corporate Finance.

"There's a huge raft of venture capital and private equity currently looking for a home," he says. "There's a lot of money looking to invest in the UK and digital is a very exciting place to be. So it's a very positive market right now. And because there's no established way of working out the value of digital companies, because the sector's so young, private equity firms, VCs and a company's competitors (particularly traditional business looking to get into digital) are willing to give very generous multiples to work out a price."

Most companies won't achieve generous multiples if they're left to their own devices, warns Hustler, because they don't necessarily know what a buyer is looking for in a new company. This is what David Richards, co-founder of Dating Direct, found. He used Clearwater to sell the company in a £27m deal in January. While he knew he and his co-founder would need to do some spring cleaning before securing a sale, he had no idea that this vital step in selling a business would be so demanding.

"We were expecting to get asked a lot of deep questions about the business, but the level of detail these guys wanted to drill down to was astounding," says Richards. "You think a few headline figures are enough, but these guys want to know every ROI on every site you advertise with. It isn't just a look at the books they're after.

"So when we were getting ready for this, it helped us work out what was and what wasn't working. Only a small proportion wasn't working, and that was mainly the smaller white-label deals we had, but the process of looking at it made us turn each situation around so we were more attractive. And it undoubtedly helped us to get the best price possible."

### Marketing attractiveness

One area that's expected to see ongoing heightened activity is online marketing and advertising. There's a new breed of mid-sized marketing firms with cash to buy small, specialist agencies, while global networks, such as WPP, are looking to fill gaps in their expertise.

"With marketing you have the enviable position of mid-sized players of 50 employees or so looking to acquire or be bought so they can belong to larger networks. Then there are the larger, global networks that are looking to acquire," says Toby Hurd, a partner at Blue Skies Acquisitions and Mergers.

"You also have VC and private equity money moving into the space because they know that's where budgets are moving," he adds. "At the same time, specialist digital agency owners either want to realise the value of their investment or know they can only expand by being bought and becoming part of a larger group."

Design and build agency Conchango is actively targeting online and mobile advertising and marketing agencies to help it grow, now that "there's more work out there than we can handle by growing organically", says Richard Poole, business consultant director. He's keen to pass


on to prospective company sellers his experience of what a buyer is looking for.

"The key thing is that a company can't have been set up just to be sold, because a potential buyer will see through that," says Poole. "The buyer will want to know for sure that a company can work without its founders, even though in advertising and marketing they'll usually be working for a set earn-out period.

"A company like ours will look for a good range of clients in different sectors, rather than a particular strong client that could up and leave. And there needs to be a strategy in place to take the company forward."

This advice is echoed by Leo Campbell, deputy chairman of Omnicom's digital network Zulu, which recently bought Weapon 7 and expects to make more purchases this year. "We're expecting a lot of activity because so many smaller digital agencies are at the stage where they can't grow without raising a huge amount to buy other agencies or being bought by large network like us," he says.

"The advertising and marketing industries have fallen in love with digital so the values ➤

**QUICK TAKE** ■ 2007 is expected to be a bumper year for the sale of new media companies, with a wealth of venture capital and private equity looking to make new investments ■ Specialist digital marketing companies are proving popular with mid-sized agencies as well as global networks ■ The best price is usually achieved through an intermediary who can advise on making the business look attractive to potential as well as target buyers ■ Prices for companies that are market leaders are high as buyers or financiers want an instant lead market share and thought leadership ■ Interest is always highest in a company that can demonstrate future growth potential and can be run without its founders

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# [Page 2 of 2]



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**Brisbourne** "The trick with knowing when to sell is estimating when your company's at about three-quarters of its potential, so there's still room for growth"

## CHEAPFLIGHTS BRINGS IN THE MIDDLEMAN

Ultimately, any middle party's main pitch to a prospective seller is that they know the market and can identify potential buyers, and that this process can be done confidentially, leaving owners to carry on running their company. This was certainly the experience of David Soskin, CEO of Cheapflights, when he sold off three non-core sites – Cheapaccommodation, Cheapholidaydeals and Cheapshortbreaks – to Internet Business Group (IBG) for £1m last year.

"We could have done it ourselves, but we wanted to use experts and were advised to go with the German company Stellant Partners," he says. "The main advantage was that they knew what a buyer would be looking for and who would be the best people to talk to. So they were able to approach people they thought might be interested who we might not have known about.

"Crucially, the whole thing was done in just ten weeks. It would have taken us a lot longer if we were combining running the company with looking for buyers and fielding queries, so we're happy. I used to work in M&As at ABN Amro, so I know that although the City gets a lot of stick, investment bankers really do know their stuff and they certainly earn their fees."

are proving attractive to owners considering selling. We've had to put in a lot of work to make deals stand up by getting our top people to appreciate that values can't be worked out traditionally because it's a new field."

This extra work to establish values is a two-way process, because often shares are offered as well as cash. "Most deals involve an earn-out period and are a mixture of cash and shares," says Campbell. "So it's very important that the companies we're buying put in the due diligence on a potential purchaser, at the same time as the purchaser is carrying out due diligence on them. They'll be getting a mixture of cash and shares, but they also want to make sure they're being given the best paper in town."

To get 'the best paper in town', financiers and company heads will agree on two things: if you're solely aimed at selling up, you won't get the best price, and the best price only comes when you can sell yourself as best-of-breed.

This is certainly Tim Brown's opinion. As a partner at venture capital firm Alta Berkeley, he has not only led investments in companies but also prepared them to be sold. Until recently he was CEO of digital marketing company Touch Clarity, in which Alta Berkeley had invested and sold to Omniture for £20m in February.

"The key is to build a brand that's known as the market leader in your target sector," he says. "Firms often pay a double or triple premium to acquire the market leader. Market and thought leadership can take you from five times revenue multiples to 15 times. Even number two in a market isn't enough. If you want to get the best price, reposition so you can be number one in your sector, and make sure someone in the firm is constantly evangelising at industry events about why you're the best."

Such evangelists and other key management people should be given share options, Brown advises, so they're incentivised to stay on once the company is sold and ensure it runs smoothly.

### Finding the best price

The constant speculation around search marketing agencies like The Search Works, Latitude and 24/7 Search shows that, if it's wanted, there's an efficient rumour mill available for anyone who's thinking of selling. But are hints or direct approaches the way to get this started, or should one go through an intermediary?

Keith Hunt, partner at Results International, which brokers deals between digital marketing company buyers and sellers (it acted for Spannerworks on its sale to iCrossing earlier this year), advises owners always to go through an intermediary. Although this may sound self-serving, he claims that those who do it agree because people selling their own companies are often misinformed about how to get the best price.

"People sometimes assume you get more if someone comes to you and you play hard to get, but the flaw is that you don't know what the rest of the market is willing to pay for you," says Hunt. "You also don't go through the process of being prepared for sale by experts before having a teaser single-page document about your company being distributed among interested parties.

"The most interested will get to find out a little more about the business until you have three or four options, from which you pick one to sign a 'heads of agreement' before agreeing final terms."

The process is standardised and designed to ensure a company is first prepared for sale before the market is fully tested, while confidential details are only seen by a truly interested party and not just someone on a spying mission.

For owners considering selling in a deal that either involves an earn-out period or will see them involved in the company somehow in the future, Michael Knott, head of strategy at Accenture's communication and hi-tech practice, has a final piece of advice. While offers on the table can be ranked by size, sellers should also consider that the highest fee usually relies on continued growth. So ensuring the purchased company and buyer get along is important.

"The constant problem for companies in an earn-out period is culture," Knott says. "It's vital to know how your people will work with their people because it's the only way growth is going to continue. It's amazing how many times people talk about purchases but then don't actually work on a strategy or assign a team of people to ensure the companies work together productively."

As 2007 shapes up to be a bumper year for acquisitions, the only thing that may hold back the market is anticipation that 2008 will be better.

"The trick with knowing when to sell is estimating when your company's at about three-quarters of its potential, so there's still room for growth to make it worthwhile for another company or private equity firm to invest," says Nic Brisbourne, a partner at VC firm Esprit.

"For a lot of the VC money that was put in a couple of years ago, that means 2007 is going to see a lot of interest. But my hunch is that 2008 will be bigger as 2007 is spent making sure companies are prepared for sale at the best price." ■

**"MARKET LEADERSHIP CAN TAKE YOU FROM FIVE TIMES REVENUE MULTIPLES TO 15 TIMES"**

Tim Brown, Alta Berkeley