

INDUSTRY EXPERTS AND GENERALIST CONSULTANTS – A HYBRID MODEL FOR MARKET DUE DILIGENCE

There are four major benefits of working with industry experts, and four benefits of working with generalist consultants. We have been collaborating with industry experts for our market due diligence engagements. By combining the best attributes of each approach, Acclaro has developed a new, hybrid model for market due diligence.

Industry Expert Benefit #1: Credibility

Given their typical stature, tenure in the industry, and role or position, industry experts bring an element of gravitas to the research process. Speaking with a small number of very experienced and knowledgeable industry experts, it is assumed, is a good substitute for making a broad swath of industry contacts.

Even if a private equity group is successful finding an expert for the specific niche sector in question, that expert is often highly biased. This bias is not the result of a nefarious attitude, but rather the natural outcome of the expert's work history. People who become industry experts have spent most of their careers in one industry. In many cases, these experts spent their entire careers in the same region of the country, working on the same products or services,

selling through the same channels, dealing with the same segment of customers, and potentially viewing reality through a narrow prism. "Where you stand depends on where you sit." In other words, all that experience may not be perfectly relevant to the niche-y industry segment in which you are considering investing.

Generalist Consultant Benefit #1 – A Clean Slate Approach to Research

While industry experts may have preconceived notions and predispositions about the market segment of interest (some of which can be outdated), consultants start with a clean slate. They begin with no ax to grind and let the data fall as it may. Objective, tangible research is best achieved by triangulating information points from numerous sources, each of which might actually be biased depending on their segment, channel, geographic region served, product/service area, etc. Only by seeing all the various viewpoints can one see which perspectives are outliers and which reflect the consensus view.

Industry Expert Benefit #2: Speed -- Industry Experts Have Answers Readily Available

One of the primary reasons cited for hiring industry experts is "to get the answers quickly." While a typical market due diligence firm may take three or more weeks to complete a study, an industry expert may provide answers in days (or hours). Industry experts have, at their disposal, answers to basic market, customer, and competitor questions. They are being asked simply to

opine on their pre-conceived notions about issues such as:

Market:

- What are the market trends and dynamics?
- What are the opportunities and threats of the market?
- How attractive is this market?

Customer:

- How loyal are customers generally?
- What are the trends associated with customer purchasing behavior?
- Are you familiar with the acquisition target? What do you think of it?

Competitor:

- Who are the competitors?
- What are the general strengths and weaknesses of the major competitors?
- What are the general trends and dynamics related to competitors in the market?

Generalist Consultant Benefit #2: Depth and Breadth

Generalist consultants often have little or no prior knowledge of the obscure niche sub-sector being studied. They are not being hired for their immediate opinions or internally held beliefs about the market in question. After all, any institutional knowledge may become a dated crutch – a liability.

Generalist consultants are researchers. The generalist consultant will find many, many different industry experts from numerous sectors, channels, geographies, and vantage points – and then look for consistencies and outliers. That basic primary research serves as the foundation for the development of actionable intelligence, analysis, options, and recommendations that follow.

Since the typical consulting team consists of approximately five individuals working on a dedicated basis over the course of a four-week assignment, the consultants can get deeply into the specifics of the industry by conducting a large number of conversations with industry participants. In addition to covering the issues that industry experts can address, consultants can also research the following:

Market:

- What is the size of the market?
- What is its growth rate?
- How does it break down into segments, by percentage?
- What are the market shares of leading participants?

Customer:

- What are the purchase decision criteria of different types of customers, prospects, and lost accounts of the target?
- How do customers rate and rank the various suppliers against their purchase decision criteria?
- How loyal are they? How likely are they to switch suppliers?
- What are customer's unmet needs?

Competitor:

- What are the strategic intentions of competitors?
- What are the opportunities that each competitor sees?
- How are they going after these presumed opportunities?
- What is the degree of competitive rivalry in the market?

Answering these questions requires real-time, quantitative and qualitative research into the market of interest. Otherwise the answers to these questions are guesses, presumptions, or insights based on historical data.

Industry Expert Benefit #3: Credibility and Rapport with Management Can Lead to Actionability

A meeting with the target company's management team is typically an appropriate first step in a market due diligence exercise. During this meeting with management, the industry expert may ask management pointed questions about the positioning of the company, and may probe management to determine their knowledge or awareness of trends and dynamics occurring in the industry.

The conversation, though focused, intense, and interrogatory, tends to be one of mutual respect. The expert is able to convey to management that, as a former operator (and not an investor nor a consultant), he is on their side. The conversation turns toward future plans, intentions, options, and the expert's recommendations. Private equity

investors appreciate the opportunity to hear the expert's opinions about how to position the company to be more profitable and to achieve a more rapid growth rate.

The downside here is that the experts are often willing to pontificate generally about tactical ideas for operational improvement, but are reluctant to express these ideas in an organized, well-structured document. Private equity groups that are awaiting a Go/No Go recommendation, action plan recommendations, or even just an analysis of what the data ultimately means for the deal or for the Company moving forward, may be disappointed. Many industry experts are averse to offering much in the way of analysis, options, conclusions, or recommendations.

Tying disparate operational tactics together into a structured, actionable strategic planning document is not what motivates the typical industry expert. Most industry experts do not produce consulting-like studies.

Generalist Consultant Benefit #3: An Attractive, Well-Written Presentation of Findings

Generalist consultants, on the other hand, are accustomed to writing detailed, well-organized, and often graphical and visually appealing reports. Lenders appreciate objective, tangible, easy-to-read summaries of the target's market positioning and the market's attractiveness.

The actionability of these reports is the result of a disciplined effort to connect tactical ideas (gleaned from interviews with numerous industry contacts) to objectives,

and ultimately to strategies. Some consultants offer specific recommendations for management to consider during the first 100 days after closing occurs.

The downside is that management may not buy into the recommendations of purely generalist consultants who have little practical experience in their industry niche. Combining the attributes of industry experts with generalist consultants creates synergy.

Industry Expert Benefit #4: Cost

Industry experts are less expensive than generalist consultants. However, industry experts typically do not conduct research; they base their opinions on the segment of the market they have observed throughout their career (which may not match the segments that the acquisition target serves). Moreover, industry experts are reluctant to provide written reports.

Generalist Consultant Benefit #4: Proven Process Results in Efficiencies

It is true that generalist consultants are more expensive than industry experts. But generalists involve a team of dedicated, coordinated researchers working along an established timeline (often three weeks), with planned conference call reviews to eliminate any surprises in a well-conceived deliverable. Research-based generalist consultants with a “clean slate” approach are typically more thorough, provide more detailed quantitative and qualitative insights, create more user-friendly reports, offer actionable recommendations, and generally

represent a better overall value to a private equity investors than industry experts.

Combining the expert model and the generalist consulting approach provides some room for cost reduction. The expert is able to help the research team of the generalist consulting practice get up to speed faster, hit the issues of highest priority more expeditiously, and focus the options and recommendations in a way that is more meaningful to management.

Conclusion

By working directly with proven industry experts – both as colleagues on the engagement team and as research contacts, the overall efficacy of the project can be improved. The concept of a hybrid model, combining the best aspects of industry experts with generalist consultants, is certainly worthy of consideration. It is clear that the downsides of each approach can each be mitigated by the opposite model.

We have a number of experts in numerous industry sectors ready to collaborate with us on a market due diligence assignment. Contact Acclaro today to learn how we combine the two approaches.

Kit Lisle is the Managing Partner with Acclaro Growth Partners, a research-based market due diligence firm located in the Washington, DC area. He can be reached at 703.434.3597 or kit@acclaropartners.com