

Buying your Competitor: Good Idea or Bad?

By Tom Marx, President and CEO of Marx Group Advisors

In my 25-years as business and marketing consultant in the aftermarket, countless times clients have asked me: "Should I buy my competitor so I can grow my business?"

There is no simple answer to this question; however, the opportunity to grow market share and increase margins and profits is even greater today given the fragile financial position that many performance retailers find themselves in during the current economy.

Some reasons to consider buying a competitor include the following:

- **Expand your geographic market**

Expanding into new markets can be more expensive and time consuming than buying a competitor. One of the biggest and most recent consolidations was the purchase of CSK by O'Reilly that was closed at the end of 2008. With the acquisition of CSK, O'Reilly Auto Parts was able to add stores in markets in the West that could have required 5-10 years of new store growth. From the perspective of time and investment capital alone, O'Reilly was able to grow into a nationwide chain in a matter of months.

The same principle applies whether you are considering expansion within your immediate community, metro or regional markets. The metrics are based on the cost of opening a new store(s) as compared to the acquisition cost of acquiring a competitor. Factors include a study of inventory, store locations, physical store configuration, revenues, margins and profits.

- **Take out a competitor**

A compelling reason to buy out a competitor is to eliminate price pressures, especially if the competitor is the low-priced leader in your market. With the competitor no longer in business, customers will have one fewer store to shop, and the opportunity to market both branded and private label products is improved.

- **Gain market share and reduce costs = more profits**

Growing market share organically can be a lengthy process. The contrast may be growing 1-2% per year vs. growing 30% in one year. The advantages can be significant, allowing you to negotiate better prices and terms with your suppliers, now that you have larger purchasing power. Increased margins will support, and could translate into, improved cash flow and more acquisitions.

- **Get valuable supplier contracts**

Sometimes your competitor may have valuable supplier relationships, one that you have wanted and not been able to obtain. These may be exclusive to your market or a certain category and may include direct imports as well as direct from US-based suppliers. These supplier contracts,

when spread across the larger footprint you have achieved through targeted acquisitions, may generate substantial revenue at higher margins.

- **Get coveted locations**

Have you ever coveted that particular street corner that is adjacent to a major shopping mall? It is the one that you drive by every day and say to yourself, “If only I had that store, I could increase my revenues by 30%.” Sometimes those opportunities never happen – unless you buy the store and convert it to your brand. Of course, you have to run the financials to ensure this is a worthwhile and a good use of your human and financial capital. Once you believe it is, then is the time to develop your acquisition strategy.

The Acquisition Strategy

Probably the most important step is *being prepared*. What does being prepared mean? It means you have done your homework and created the background preparations so that when an opportunity becomes available, you are ready to go for it.

- **Business and financial statements are in order**

We have watched great opportunities fall apart when the buyer has not gotten their financial statements in order and procured an agreement from the local bank, or some other equity partner, before making a move to buy a competitor. The acquisition process always drags the skeleton out of the closet for the target as well as yourself as the financial, legal and investment people become involved. If you are even just considering an acquisition, treat this transaction the same as you would as a purchase of real property in today’s market: get pre-approved credit. The acquisition candidate will know you are serious and not only will you save a lot of time, you can often negotiate a better deal, especially when offering “all cash.”

Key elements include: keeping your tax returns and financial statements current, understanding the impact the acquisition will have on your cash flow, and getting the money needed for the acquisition pre-approved.

- **Future Think - Understand current and future market trends**

An acquisition can turn into a financial debacle if you are not a visionary about the direction the markets or products are heading. For companies in the performance truck sector, just think of the growth you would have experienced if you had predicted the explosion of this market 10-12 years ago. Conversely, if you had not foreseen the more recent decline of the performance truck market over the past 12-18 months, an acquisition in that sector could be putting your core business at jeopardy.

Another example of “Future Think” is the current economy, which has caught many performance retailers by surprise. A year ago, the OE replacement part market was crashing and the performance markets were booming. Today the opposite is true in many aftermarket niche sectors. By paying attention to market trends, you can dramatically increase the return on your investment.

- **If merging, be very clear on the risks and rewards**

While there are many different types of acquisitions (and these will be covered in a subsequent article), one decision you need to make in advance is whether you seek a merger or an acquisition. The strategies are profoundly different.

In a typical merger, you are often creating a partnership with the company. A merger does not necessarily mean a “merger of equals.” The acquired company may become a minority owner in the new enterprise. The role of the current owner may entitle them to decision-making power and grant some level of authority in the new entity.

In a typical acquisition, you are acquiring the other company and the future of the previous owner is yours to negotiate. Often the owner stays on for a period of time as a consultant. In some cases, the owner may stay on to manage a division or even the entire company.

In either case, take a hard look at your nature and personality and decide how willing you are to share or give up control. And then base your acquisition strategy accordingly.

By using a merger and acquisition consultant to help guide you in this process, you have the opportunity to avoid many of the pitfalls that can occur during the M&A process. I have observed both successes, and some failures. The failures have always been related to either a poor strategy, or poorly executed integration after the acquisition has closed and money has changed hands. As with most endeavors in life, the difference between success and failure begins with being prepared and informed, and your ability and willingness to be flexible and accept change.

About Marx Group Advisors:

Tom Marx is the president and co-founder of Marx Group Advisors (MGA), a mergers and acquisition specialist focused on providing M&A services to the Automotive and Heavy Duty aftermarkets.

Tom, and his partner, Paul Cooperstein, represents sellers and buyers of companies and provides consulting services that enable companies to improve their balance sheets before beginning the M&A process, as well as post-M&A integration. MGA also represents private equity firms when financing is a part of the transaction.

Marx Group Advisors (www.marxgroupadvisors.com) is headquartered in San Rafael, CA, and has offices in Boston, MA and San Rafael, CA. MGA is a division of The Marx Group (www.themarxgrp.com), a 25-year old Marketing Communications Company that specializes in the Automotive and Heavy Duty Aftermarkets and has offices in San Rafael, Nashville, Chicago and New York. Tom is an active member of SEMA, AAIA, AASA and APRA. He is past vice chair of the AAIA Marketing Communications and Member Relations Committee and is past president of the Automotive Communications Council.