Which exit strategy is right for you and your business?

Baby boomers account for approximately 21% of the U.S. population — and 70% of baby boomer business owners will be retiring in the coming years. According to Fast Company, baby boomers currently own about 2.9 million businesses. What will happen when a large wave of boomers retire and millions of businesses of all sizes suddenly flood the market? And do these business owners have an exit strategy in place?

The reality is that many of them don't, which could mean they won't be able to extract the value they want in an oversaturated M&A climate in an unpredictable economy. That's why it's important for business owners to consider potential exit strategies as well as key steps for their retirement to maintain the value and legacy of their business — and to work with a trusted financial advisor to ensure they are prepared.

Before considering potential exit strategies, it is important to evaluate personal, financial and business readiness. Common issues business owners face when determining their exit planning readiness include not having a contingency plan or formal transition team, missed alignment of their personal life goals, risk sensitivity considerations and the ability to forecast performance and business predictability. After evaluating their readiness with an advisor, they can move forward with aligning on the best strategy for their situation.

Choosing the Right Exit Planning Strategy

Transition to Family

Benefits: This option may enable continuity for the business, its operations and the customer experience — especially if the chosen family member is already working in a leadership position. It may also facilitate a sense of comfort for all involved, knowing the business will be in the hands of a successor who has an intimate understanding of its operations. If the transaction is part of a broader estate plan, there may also be tax advantages linked to the transfer of wealth to family.

Considerations: There may be more than one potential successor or family member who want to be made key decision-makers but are not capable of leading the business. A business transfer to family can also have significant tax consequences, and if transferred during the owner's lifetime, there may also be financial complications that could impact the owner's retirement.

Choosing the Right Exit Planning Strategy (cont'd)

Sell to an Investor

Benefits: The business potentially gets an infusion of capital, ownership gets a partial payout and leadership has continuity of compensation income because investors typically require current ownership and management to stay on. While financial buyers like private equity groups may lack expertise in a specific industry and cannot add valuable infrastructure or insight, they do provide additional capital for expansion and growth — in exchange for future profits.

Considerations: It is important that ownership and management are both part of developing the vision that is sold to investors, because if they lack the desire to deliver that vision, it can have serious consequences for the business and its employees.

Sell to Business Partners or Management

Benefits: This can help secure continuity for the business and reduce the risk of operational shifts that could impact profitability or market share because partners and management are typically well-known among stakeholders. If a buy-sell agreement is in place and an understanding exists between the buyer's role and current ownership, selling to partners or management can be a smooth and fairly swift transition.

Considerations: Managing down potential conflicts, and subsequently risks to the business, requires a slow and thoughtful approach. There may be financial complications depending on the structure of the sale. Should the buyer lack capital for the purchase, outside resources or insurance may need to be secured.

Sell to an Industry Buyer

Benefits: Industry buyers should have the infrastructure and management to absorb the business and keep it moving. Competitors may be willing to pay top dollar, whether they're trying to eliminate competition or grow market share. If so, the seller gains leverage at the negotiating table, which could mean securing attractive terms outside of the final price.

Considerations: Stakeholders that may have helped shape the business into what it is will have no say in its future — nor take income from it. While not foolproof, a mutual agreement followed by an information exchange that requires buyers to share confidential information can help protect the business.

With a growing number of business owners expected to retire in 2024 and beyond, working with a professional advisor to discuss exit strategies is more important than ever.

At Texas Capital, our advisors help clients maximize the potential to build and protect their legacy across all phases of their business, including exit plans. With deep industry experience and an understanding of how capital markets work in each field, they can help clients develop customized plans for life during and after the transition.

Click here to meet with your Texas Capital advisor or to schedule a meeting with an advisor in your area. We're committed to serving families across generations, helping to preserve family legacies.

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