

2020

Search Fund Study

Selected Observations

This 2020 study reports on the financial returns and key qualities of 401 search funds formed in the United States and Canada since 1984. It presents data as well as analysis from surveys regarding search funds formed, companies acquired as a result, and financial returns from them as of December 31, 2019, along with new analysis of acquisitions and seller demographics.

As background, since 1996 the Center for Entrepreneurial Studies at Stanford Graduate School of Business has conducted a study every two years on search funds, an entrepreneurial path undertaken by one or two individuals who form an investment vehicle with a small group of aligned investors to search for, acquire, and lead a privately held company for the medium to long term, typically six to ten years.¹ Through this research, Stanford seeks to provide insight into the factors that influence the outcomes of these entrepreneurship vehicles for first-time searcher-CEOs and their investors. This survey includes data from every known (traditional) search fund in the United States and Canada.

Peter Kelly, Lecturer in Management, and Sara Heston, Assistant Director, Search Fund Project, Stanford Graduate School of Business, conducted this study.

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¹ This study focuses on search funds formed by a first-time searcher and funded by a group of investors, termed herein “traditional search funds” or “search funds.” Other forms of search funds exist, such as searches that are self-funded or funded by a single entity, as noted in **Appendix C**.

Executive Summary

With a record number of funds launched and acquisitions made in 2018 and 2019, the search fund community is robust and growing. Data from this 2020 study shows that search funds continue to provide some entrepreneurs with a relatively fast path to becoming an owner-CEO and investors with attractive financial returns and mentoring opportunities.

A record 88 search funds launched during 2018 and 2019. Demographics of the searchers were similar to previous studies, although searchers came from a wider variety of academic backgrounds, and more of them employed a deep-dive search strategy than a high-volume approach. Average time to complete an acquisition remained at 23 months, which is longer than in studies prior to 2018, and the percent of searches ending without an acquisition increased, from 31% to 33%. Women accounted for 7% of searchers. We do not have data on the race and ethnicity of searchers in this study but intend to collect it in future studies. Shifts in the industries of acquired companies continued, with various segments of Healthcare, Software, and Services gaining popularity. Additionally, the size of deals fell, with median acquisition price declining to \$10 million after years of increases, while the median EBITDA multiple paid remained stable at 6.0x (the purchase price as a multiple of EBITDA at acquisition).

From 1984 through 2019, at least \$1.4 billion of equity capital was invested in traditional search funds and their acquired companies, up \$475 million from the last study, generating, in total, approximately \$6.9 billion of equity value for investors and an estimated \$1.8 billion for entrepreneurs so far. The aggregate pre-tax internal rate of return for investors was **32.6%** through the end of 2019, down from 33.7% in the 2018 study, and the return on invested capital was **5.5x**, down from 6.9x in 2018, reflecting slightly lower returns, shorter hold periods, and a record number of new acquisitions. Of note, IRRs excluding the top 5 returning funds continue to increase, perhaps indicating that on average better companies are being acquired and developed (**Figures H and I**).

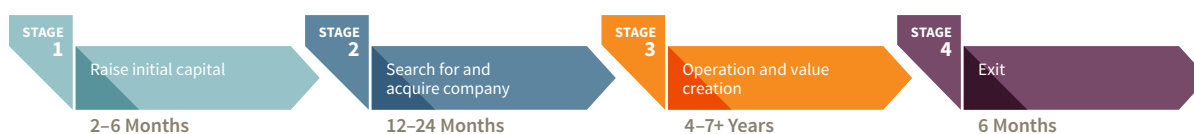
We collected new information on searcher strategy and seller demographics, reported in more detail on page 5 and page 7, respectively. As in the 2018 study, we present search, acquisition, and exit activity, followed by analyses of financial returns, and then search-acquired company characteristics. Finally, presented are summary observations from IESE Business School's sister study on search fund activity outside of the United States and Canada.

What Is a Search Fund?

A search fund is an entrepreneurial path undertaken by one or two individuals (the “searchers”) who form an investment vehicle with a small group of aligned investors, some of whom become mentors, in order to search for, acquire, and lead a privately held company for the medium to long term, typically six to ten years. When successful, this has resulted in a relatively fast path to becoming an owner-CEO, attractive financial returns for both investors and searchers, and growing, well-run enterprises.

The term “search fund” originated at Harvard Business School in 1984, was popularized at Stanford GSB in the following 10 years, and has spread steadily to business schools and entrepreneurs around the world. A typical search fund progresses through four stages:

FIGURE A | THE SEARCH FUND LIFE CYCLE



A detailed explanation of the search fund model is included in **Appendix A**, beginning on page 27. Also, Stanford’s Search Fund Primer² more deeply examines the formation, search, and acquisition stages from the perspective of the entrepreneur.

Survey Results: Fundraising, Search, and Acquisition

This study includes 401 first-time search funds formed since 1984.³ In keeping with previous studies, we excluded funds led by principals who had previously raised a search fund, who self-funded their search, or who pursued their search with a single search sponsor.⁴ While those forms of search are noteworthy and mentioned later in **Appendix C**, historically they have not been included in this study. The focus of this research is on the characteristics and returns of investing in a first-time search fund entrepreneur with a group of aligned advising investors.

For each search fund, we collected information on the backgrounds of the principals, as well as key fundraising, acquisition, company, and valuation metrics. We worked to include all known traditional search funds.⁵

2 Readers can find the *Search Fund Primer* on Stanford GSB’s Center for Entrepreneurial Studies site: <http://www.gsb.stanford.edu/faculty-research/centers-initiatives/ces/research/search-funds/primer>.

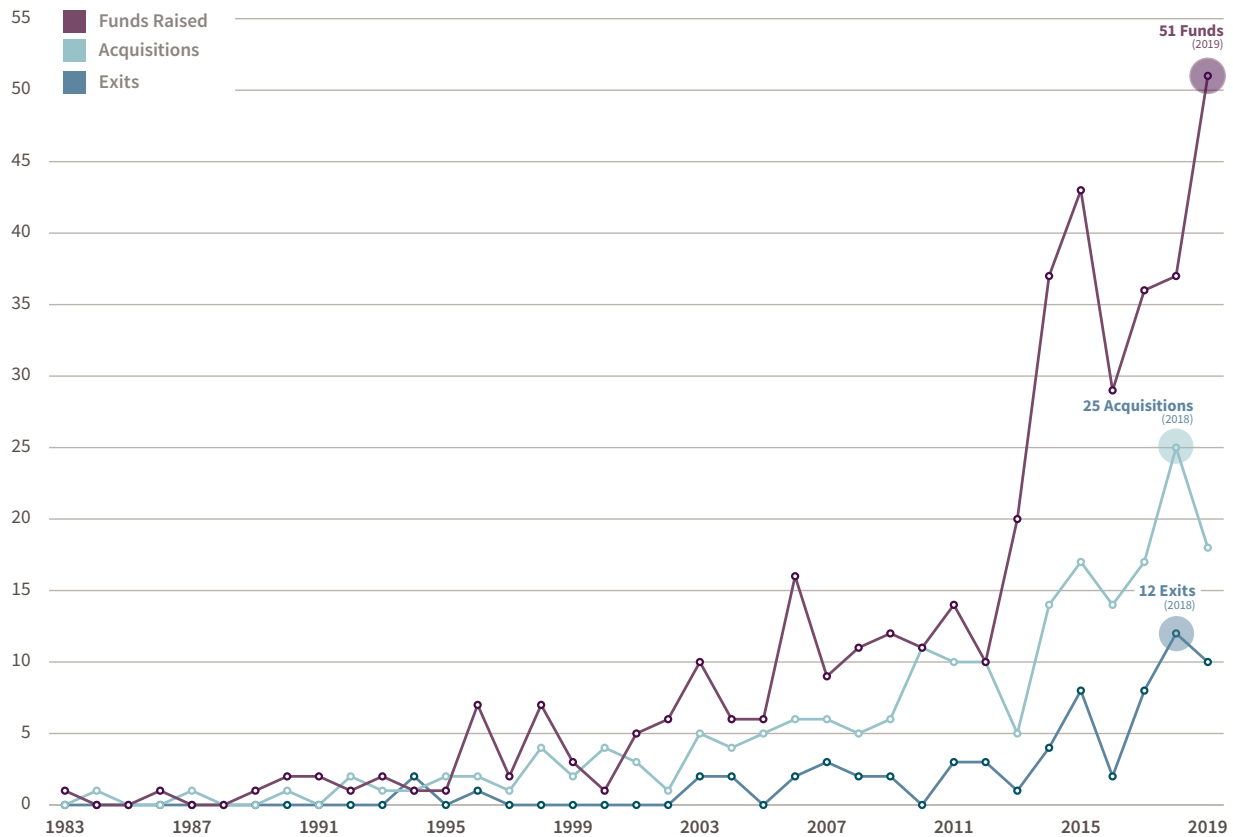
3 These include every known search fund and acquired company in the United States and Canada. Note that due to historical analyses, data through 2009 includes international search funds, tracked thereafter in IESE’s sister studies on International Search Funds.

4 Serial, self-funded, and single-investor search fund entrepreneurs have track records that imply different fundraising, management, and operating approaches, as well as distinctive networks of investors, intermediaries, and sellers. See “Alternative Search Fund Models” in **Appendix C** for more information.

5 We gathered complete data on all 204 search funds that acquired companies and included 186 in our aggregate financial analysis, excluding 18 companies that had been operating for less than one year.

The number of search funds raised, acquisitions made, and exits have all trended higher over the last two years, as seen in **Figure B**. After a slowdown in 2016, the number of new searchers has steadily risen for the past three years to a record of 51 new searchers in 2019.

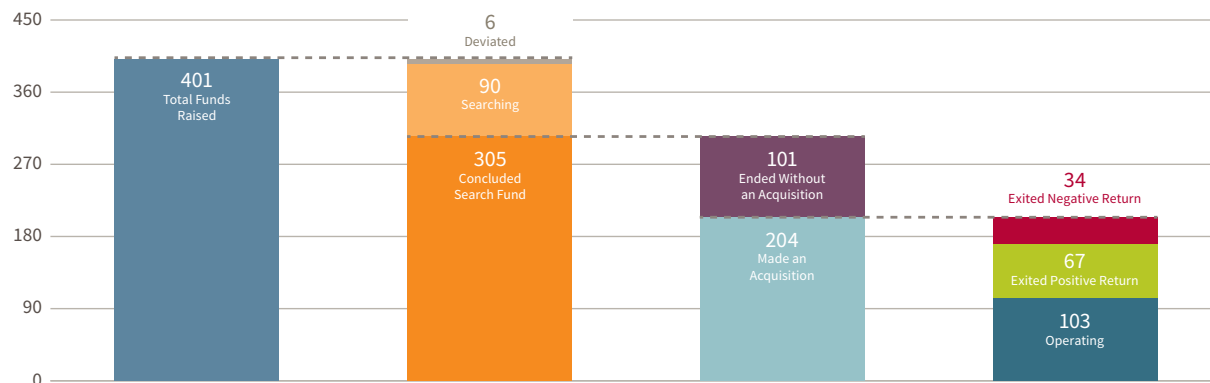
FIGURE B | SEARCH FUND ACTIVITY BY YEAR



Source: Data from Stanford GSB search fund surveys.

Details on the status of all funds as of December 31, 2019, are shown in **Figure C**. There were 90 actively searching funds at that time, a 5% increase from December 31, 2017. Of the 305 funds no longer searching, 101, or 33%, closed without making an acquisition. The remaining 204 searches successfully acquired companies, 43 more than at the end of 2017. Of those that made an acquisition, 22 exited with a positive return in either 2018 or 2019, a significant increase over 10 in the previous two-year study period. Further outcomes are described in the Returns section on page 7 and **Figure F**.

FIGURE C | ALL SEARCH FUNDS BY STATUS



Source: Data from Stanford GSB search fund surveys.

Profile of Principals⁶

Searcher demographics have remained consistent over the last several years, as detailed in **Exhibit 1**. Notable developments in searcher backgrounds (**Exhibit 2**) include a slight increase in investment banking backgrounds, a decrease in private equity backgrounds, and steady increases in searchers with general management backgrounds.

Women continue to remain underrepresented in search funds, accounting for 7% of individuals that began searching in 2018 or 2019. Eighty-four percent of searchers have an MBA. The number of searchers launching a fund within three years of business school graduation increased from 44% in the 2018 study to 62% in this study, and the median age of a searcher was unchanged at 32.

Fundraising and Search

As seen in **Exhibit 3**, the median amount of capital raised per principal in the last two years was \$429,000, an 8% increase from the prior study period. The median time to raise a fund and number of investors have been consistent at three months and 15 investors, respectively, for the past six years.

Exhibits 4A, 4B, and 4C present the industries targeted by searchers. Industries more frequently targeted include Software, Tech-enabled Services, Education, Healthcare “Providers” (companies that provide healthcare services directly to individuals) and “Services to Providers” (companies that sell goods and services to Healthcare Providers rather than to individual patients), and Financial Services.

The Acquisition

Prospecting

Most searchers opt for either a high-volume, opportunistic search that canvases a multitude of industries or a deep-dive search with a strong focus on specific industry segments. Although nuanced approaches lie within these two broad categories, and search strategies can change as a search progresses, most searchers identify primarily with one style or the other. In the 2020 study, we collected data on search style for the first time and found an even split. Fifty-two percent of recent searchers took a deep-dive approach, an increase from 41% of searchers who did so in 2016 and 2017.

⁶ We have not collected data on searcher ethnicity in recent surveys but see this as a key area for future study.

The median number of companies identified as a potential target by recent searchers in this study decreased again, as it had in the last study, from 386 to 285. The increased portion of searchers taking a deep-dive approach partially accounts for this. In the 2018 and 2019 period, high-volume, opportunistic searchers identified a median of 500 companies, compared to a median of 140 for deep-dive searchers.

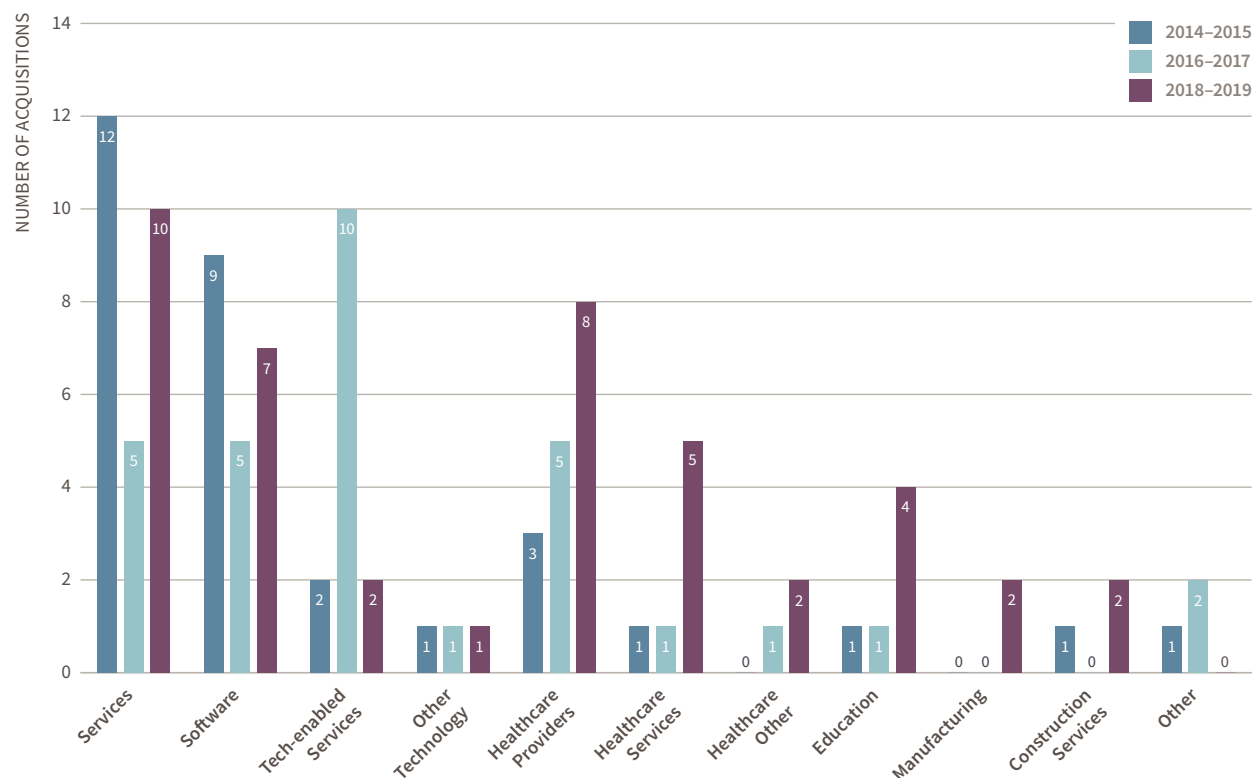
Acquisition Metrics

Search funds acquired somewhat smaller companies in the last two years. After six years of consistent increases, the median purchase price of a search-fund-acquired company decreased in the 2018 and 2019 period, from \$13.1 million to \$10 million. Median revenue for acquired companies dropped to \$6.3 million in 2018 and 2019 from \$10 million in the prior study period, and median EBITDA of \$1.8 million was lower than prior periods. The median EBITDA multiple paid remained in line with prior periods at 6.0x (**Exhibits 5 and 6**).

Industries

Figure D presents detail regarding the industries of businesses actually acquired. Thirty-five percent of acquisitions made in 2018 and 2019 were in various healthcare industries, including eight Providers (services to patients) and five Service Providers (services to healthcare providers, not directly to patients). Various technology industries, primarily Software and Tech-enabled Services, continued to be areas of regular acquisition, as did Services, a broad sector that encompasses a multitude of business-to-business products and services.

FIGURE D | INDUSTRIES OF ACQUIRED COMPANIES⁷



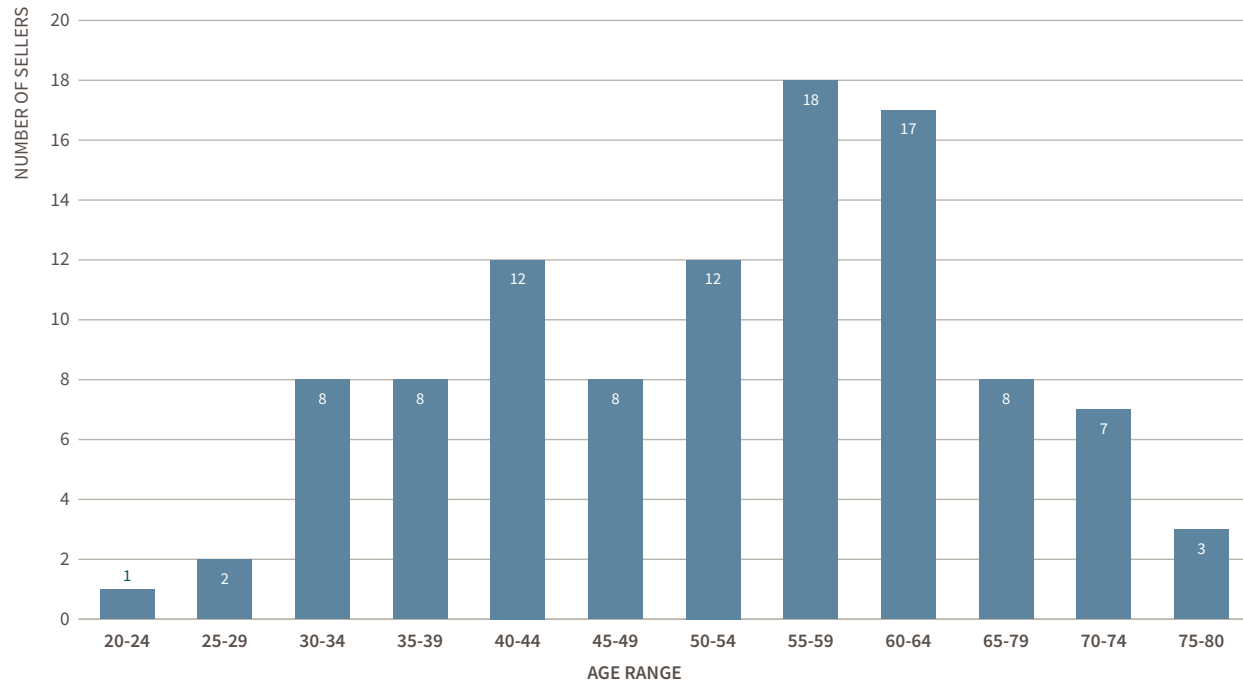
Source: Data from Stanford GSB search fund surveys.

7 The “Healthcare Other” classification includes devices, pharmaceuticals, insurance, and other healthcare-related businesses.

Seller Demographics

For the first time, we collected data on the sellers of businesses acquired by searchers. While sellers have been predominantly white and male, there is a wide age range, charted in **Figure E**. This distribution suggests that sellers can come from any generation and may have various motives for selling. Also, sellers have typically been well-educated, with 76% having a four-year college degree or higher and 21% having a high school diploma.

FIGURE E | AGE OF SELLERS (N = 104)⁸



Source: Data from Stanford GSB search fund surveys.

Financial Return Method

The method of calculating returns did not change from the previous study and is described further in **Appendix B**. It measures returns based on capital investments from and distributions to the original search fund investors investing in both the search and acquisition phases, but not follow-on investments.

Returns

In the 2020 study, the ROI for all known investments decreased to 5.5x, from 6.9x in the 2018 study. This is partially the result of the high number of recent acquisitions and the inclusion of new data on some older funds.⁹ The aggregate IRR of 32.6% declined slightly from the 2018 study IRR of 33.7%. The IRR excluding the top 5 returns increased for the fifth study in a row, to 28.5%, while the ROI excluding the top 5 funds decreased slightly, from 3.0x to 2.9x.

The IRR for funds has remained consistently between 32% and 38% since the 2001 study, but the range of individual returns, as well as the holding period, has varied significantly.

⁸ This analysis is based on buyer-reported data.

⁹ This new data on older funds includes a few companies with disproportionately lower returns. Data on seven companies with previously insufficient data was obtained and included in calculations and returns for three exited companies were adjusted (lower) to reflect new information. This bias should be entirely corrected with the current study's high response rate; extra effort and cooperation within the community during the last two studies have resulted in data being collected from virtually every known search fund and acquisition.

In the current study, 67% of all searchers made an acquisition. This is down slightly from 69% in the 2018 study and 73% in the 2016 study. About 60% of searchers that began searching in the past six years have made acquisitions, accounting for the decrease in the overall percentage. The 2020 survey data indicates a wide range of success acquiring a company. Common wisdom among long-term search investors holds that some searchers are significantly more likely to acquire a company than others because they are (a) better prepared, (b) more suited for search, and (c) have better search networks and mentors. If so, searchers may increase their odds of success by (a) studying and grasping key lessons of past searches thoroughly, (b) assessing their own qualities and motivations deeply before deciding to search, and (c) forming or accessing deep and strong networks of previous search entrepreneurs and investors adept at supporting searchers and new CEOs.

Key lessons from past searches are perhaps best learned in business school classes dedicated to search funds, from recent searchers, and from experienced search investors, advisors, and mentors. The amount of published material regarding how to best do a search is growing steadily, such as the Stanford Search Fund Primer, and primary research about these lessons can be invaluable in deciding whether to pursue a search, how and with whom to do so, what sort of company to buy, and how to run it.

Of those that made an acquisition, 75% achieved a gain in equity value, an increase from 71% in the 2018 study. This data indicates that fewer searchers completed acquisitions and those that did stood a better chance of success. **Figure F** shows the percentage of funds in each phase of the cycle, as well as return characteristics for exited funds. For distributions of funds by ROI and IRR, see **Exhibits 7** and **8**, respectively.

FIGURE F | SEARCH FUND OUTCOMES¹⁰



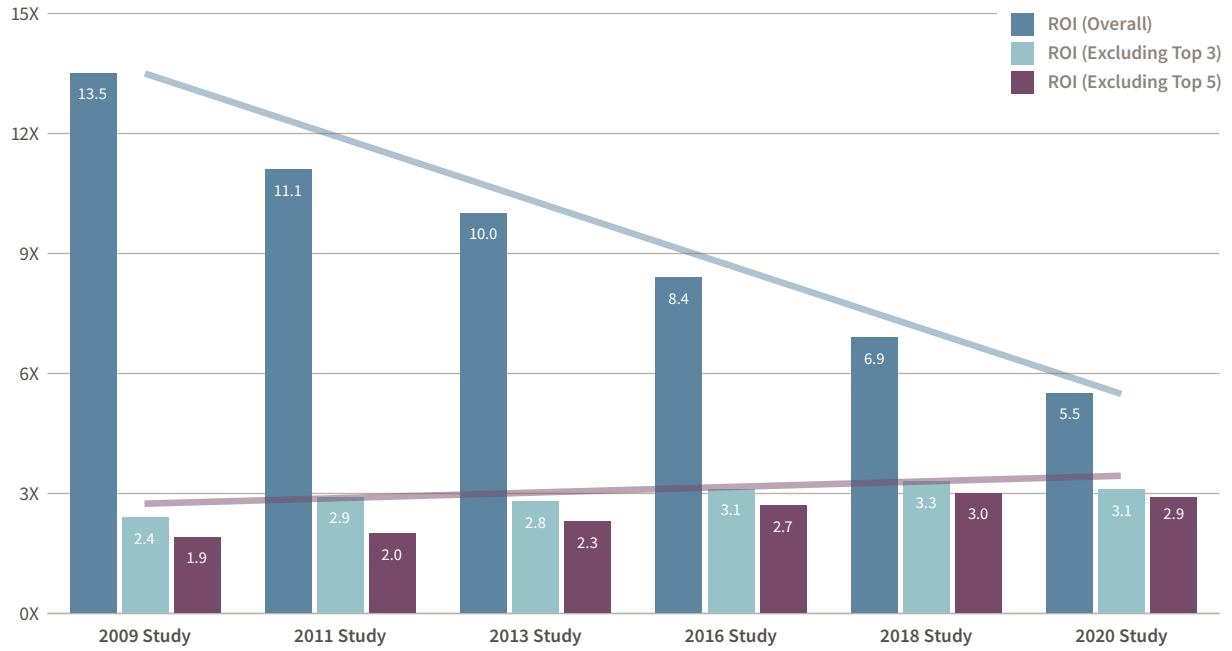
Source: Data from Stanford GSB search fund surveys.

For each category, we include the percentage of exited investments and operating companies, as well as median hold times. For example, the upper boxes in the right-hand column of **Figure F** indicate that of companies in the “1-2x Return” category, 82% are operating and 18% are exited, and that the median hold time for each was 3.1 years and 5.5 years, respectively.

A small number of highly successful search funds disproportionately increase the aggregate returns, as in other risk capital portfolios. A notable trend in this study is that the IRRs excluding the top 5 performers have increased, reflecting a larger number of high-return (i.e., greater than 5x ROI) search funds. For returns adjusted to exclude the top 3 and top 5 performers, see **Figures G** and **H**.

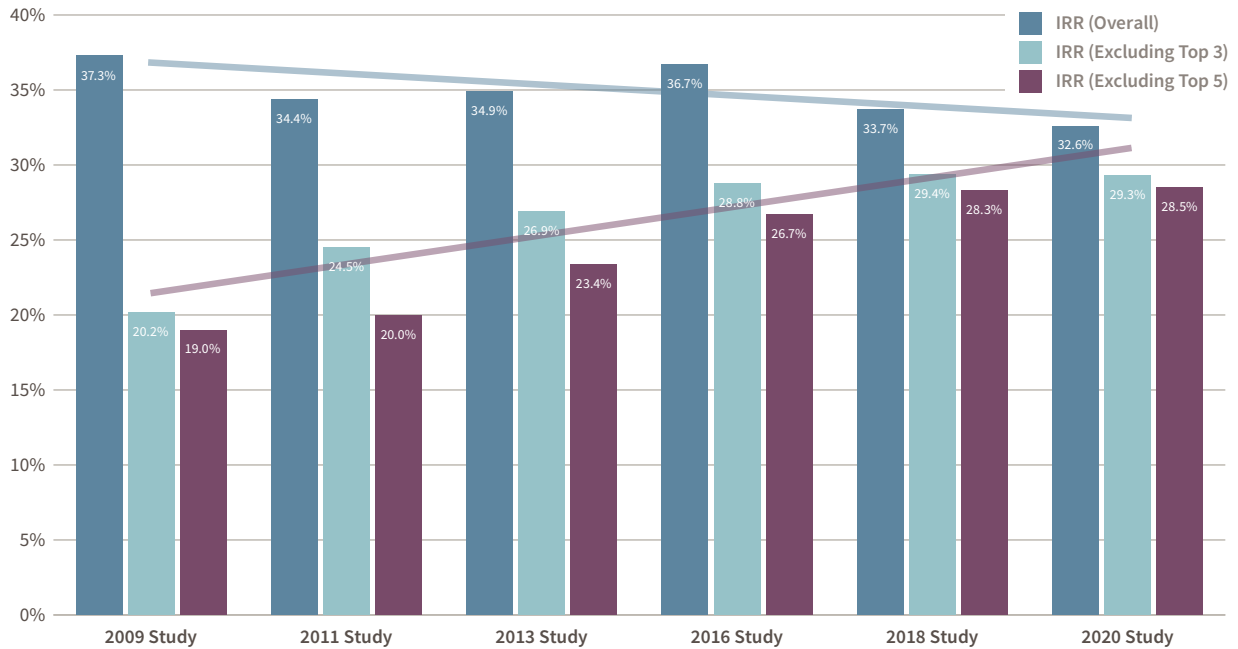
¹⁰ The gain and loss categories in Figure F exclude 18 companies operating for less than one year as of December 31, 2019. For a select few companies, the exit event is based on original investors selling a majority of their interest.

FIGURE G | AGGREGATE SEARCH FUND ROI (2009–2019)



Source: Data from Stanford GSB search fund surveys.

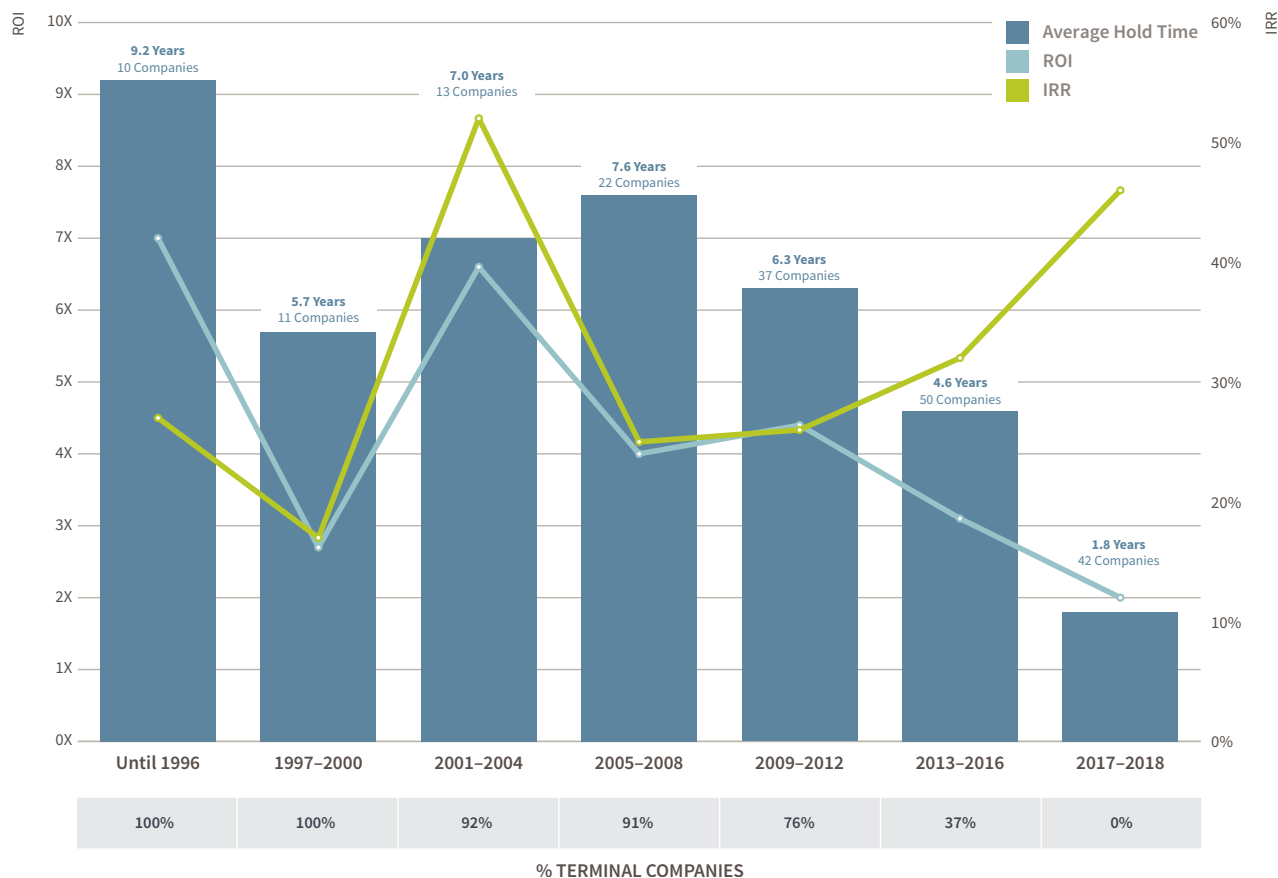
FIGURE H | AGGREGATE SEARCH FUND IRR (2009–2019)



Source: Data from Stanford GSB search fund surveys.

For insight into how returns have varied with timing, we present IRR and ROI by year of acquisition in **Figure I**. The companies operating for the shortest amount of time have lower ROIs as a result of their brief operating period. They also account for a larger portion of companies in the study, which results in a lower overall ROI for the group. On the positive side, these newer acquisitions report valuations leading to higher IRRs, suggesting they are off to favorable starts.

FIGURE I | IRR AND ROI BY YEAR OF COMPANY ACQUISITION (N = 185)¹¹



Source: Data from Stanford GSB search fund surveys.

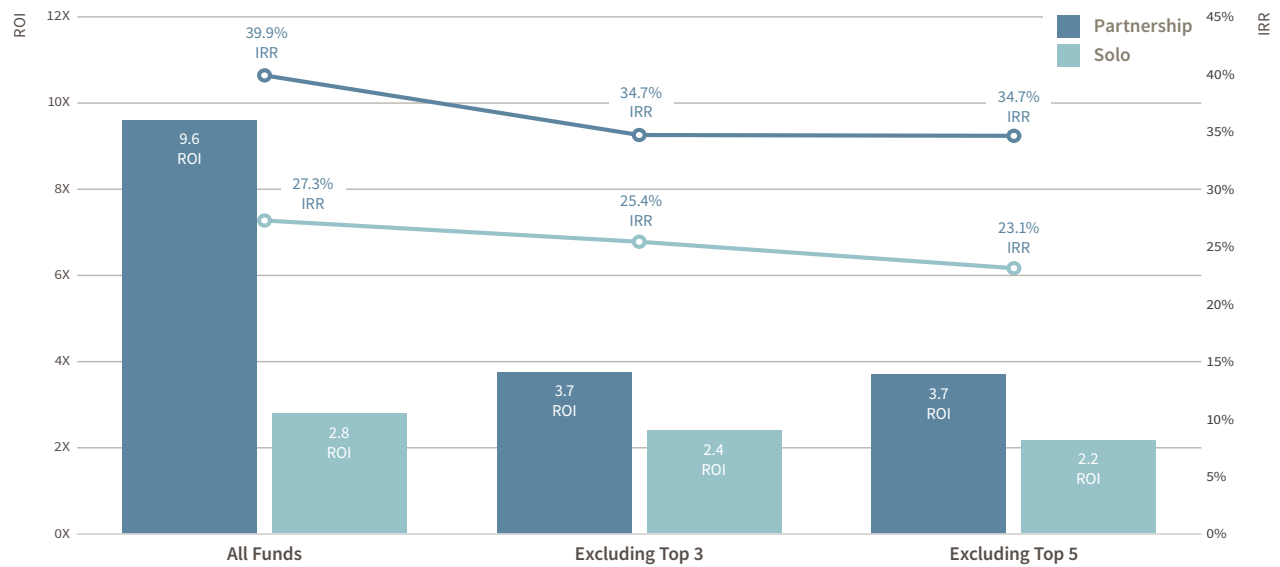
Partnership Status

In the 2020 study only 20% of searches were formed by partners, compared with 45% in 2016 and 2017. Data continues to support the claim that partnerships achieve higher returns, although there is no certainty that the partnership approach led to the higher returns.

¹¹ The top-performing fund was excluded from this analysis in order to observe underlying trends. In addition, by definition the analysis presented here includes only data from search funds that completed an acquisition, and not from search funds that terminated without an acquisition. As such, this analysis is not directly comparable to the overall analysis of search fund returns that includes terminated searches. In the overall data, the inclusion of terminated searches decreases IRR by approximately 150 basis points. For reference, removing the top-returning fund from the other cohorts in this chart, besides removing the top-performing fund as mentioned above, only meaningfully lowered returns in the 2001-2004 cohort. The others decreased but not significantly.

FIGURE J | ROI AND IRR BY PARTNERSHIP STATUS

(N = 186, INCLUDING 108 SOLO SEARCHES AND 78 PARTNERSHIPS)¹²

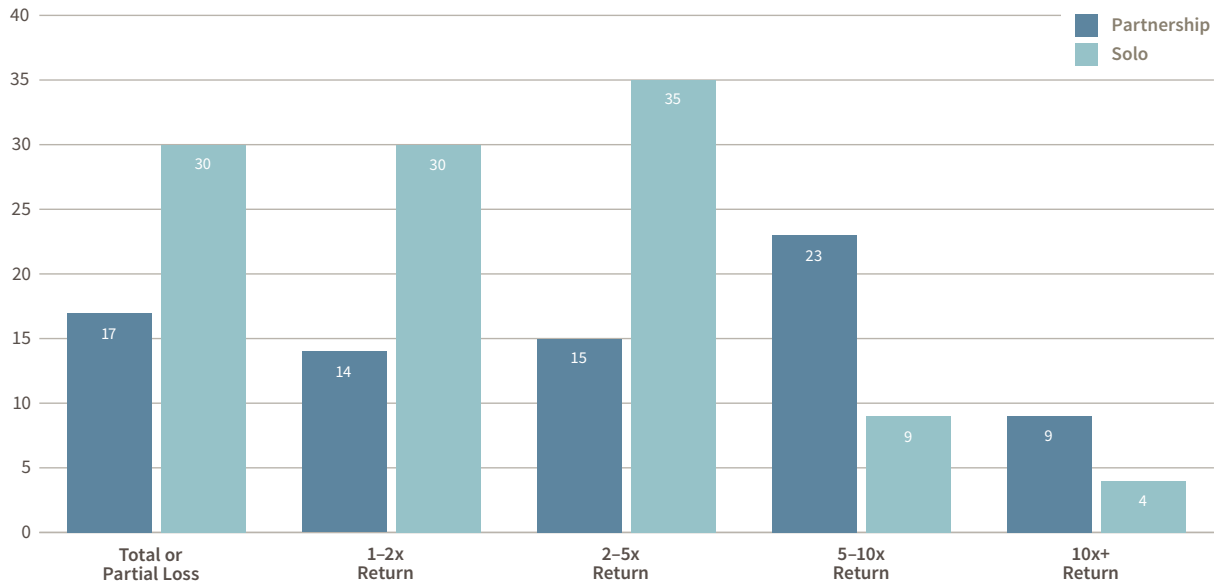


Source: Data from Stanford GSB search fund surveys.

Among all funds that made an acquisition, 42% were partnerships and 58% were solo searchers. Partnerships, however, accounted for 68% of companies with an ROI greater than 5x and only 37% of investments with a negative return.

FIGURE K | ROI BY PARTNERSHIP STATUS

(N = 186, INCLUDING 108 SOLO SEARCHES AND 78 PARTNERSHIPS)¹²



Source: Data from Stanford GSB search fund surveys.

¹² This evaluation included all funds that had made acquisitions (both currently operating and exited) at least one year prior to December 31, 2019. Funds that were searching for an acquisition, had concluded as an unsuccessful search, or had not been operating for one year as of December 31, 2019, were not considered.

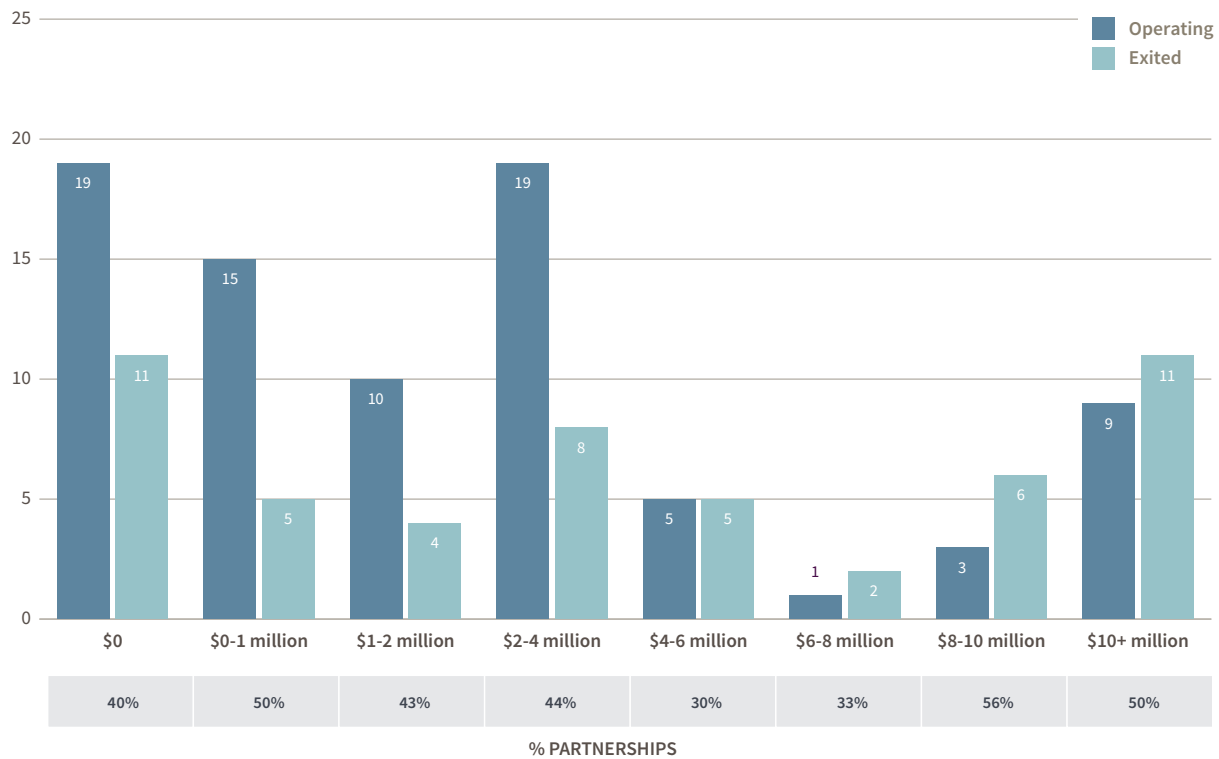
Salary and Equity Compensation for Entrepreneurs

We collected compensation data on 131 search fund entrepreneurs who acquired their companies prior to December 31, 2018. Of those, 79 were still operating and 52 had exited. While this does not capture all entrepreneurs' data, upon examination it appears to be a large and diverse enough sample to accurately represent the aggregate.

Accounting for partnerships, the average equity value for each entrepreneur still operating a company is \$4.36 million, a decrease of \$1.27 million from the 2018 study. We believe this is because of the high number of recent acquisitions that are early in the cycle, in part since the amount of equity per year of operation is unchanged from the 2018 study at \$1.47 million. Entrepreneurs who exited their business earned equity averaging \$6.47 million with a per-year value of \$1.25 million, both in line with the 2018 study.

The median equity value for current operators in the 2020 study is \$1.07 million, and \$0.54 million per year of operation. Those that exited earned a median equity value of \$3.25 million and \$0.67 million per year of operation.

FIGURE L | ENTREPRENEUR EQUITY EARNED (N = 133 COMPANIES)



Source: Data from Stanford GSB search fund surveys.

Figure L shows the distribution by company. There were 32 companies led by 48 entrepreneurs with equity value of \$6 million or higher (32 in partnerships of two, and 16 individual searchers).

Current Compensation

Searcher Compensation

We collected data from 180 individual searchers who began their search from 2013 to 2019. Of these, 98 searchers representing 82 funds were actively searching as of December 31, 2019. The range of annual salaries during the search phase was \$30,000 to \$200,000, with a median (and mean) of \$110,000 and no bonus.

CEO Compensation

This data set was reported by 124 of the 179 CEOs who acquired their companies between 2003 and 2019 and includes data for both exited and currently operating companies, with results similar to 2018.

The range for CEO base salary was \$120,000 to \$750,000, with a mean of \$217,722 and a median of \$200,000. The range for the annual bonus was \$0 to \$700,000, with a mean of \$59,019 and a median of \$50,000. The range of total CEO compensation (base salary plus bonus) was \$120,000 to \$1.45 million (an outlier), with a median total compensation of \$253,500.

In general, CEO compensation increases the longer the company is held, as one might expect with company growth and longer CEO tenure; however, the range of increase is small. A CEO in year two makes on average \$237,000 compared with a CEO in year eight, who makes an average of \$304,000. We also analyzed CEO compensation in relation to the size of the company and found little correlation, suggesting that company size does not have a large influence on CEO salary (although some longer-tenured and larger-company CEOs have significantly higher salaries).

Acquisition Characteristics

The 2020 study continued to examine how company and industry characteristics correlate with returns. We collected and analyzed data from companies operating for at least a year regarding recurring revenue and industry growth.

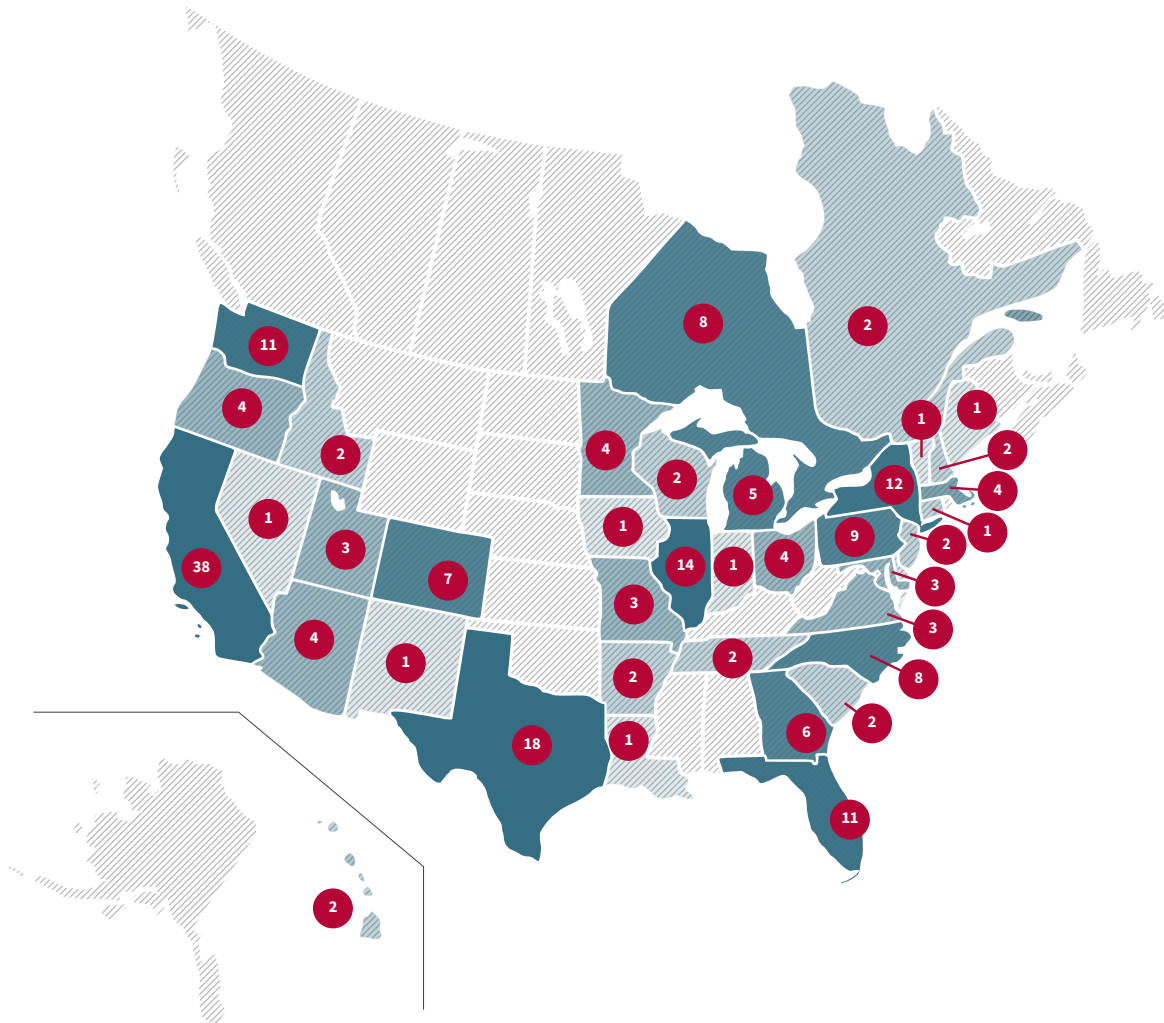
Eighty-three percent of searchers acquired businesses in industries they expected to grow at 3% or greater for three to five years after acquisition, with only 17% targeting lower-growth industries. Little correlation could be found between expected industry growth and returns. The actual growth rate experienced and industry definition can differ in reality, perhaps accounting for the lack of apparent connection between industry growth rate at acquisition and returns.

Recurring revenue is often sought by investors and entrepreneurs, with 55% of searchers acquiring companies for which recurring revenue represents greater than 65% of total revenue. However, little correlation was evident between high recurring revenue at acquisition and returns. This analysis may be skewed by characterizing revenue at acquisition rather than exit, or by applying a narrow definition of recurring revenue. We plan to continue to work to better understand this relationship.

Geography

In the 2020 study, we continued to track the relationship between where an entrepreneur searches from and the location of the company they acquire.

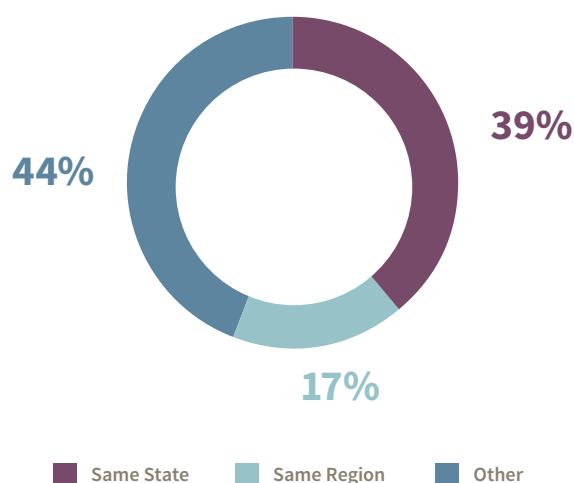
FIGURE M | ACQUIRED COMPANIES LISTED BY STATE (N = 205)¹³



Source: Data from Stanford GSB search fund surveys.

13 For simplicity, "State" is used to name this chart, although two Canadian provinces are also displayed.

FIGURE N | LOCATION OF SEARCH FUNDS VS. THE COMPANIES THEY ACQUIRE (N = 205)



Source: Data from Stanford GSB search fund surveys.

Thirty-nine percent of searchers bought companies in the same state as they searched, 17% purchased companies in the same region (defined as adjoining states), and 44% bought companies in an other region (outside the one in which they searched), as in **Figure N**.¹⁴

International Search Funds

In 2011, as a result of the growing number of search funds outside of the United States and Canada (e.g., Latin America, Europe, Asia, and Africa), Stanford GSB partnered with IESE Business School in Barcelona, Spain, to report on international search funds.¹⁵ International search funds raised prior to 2010 remain part of the record retained herein but were not included in the Stanford data after 2009.

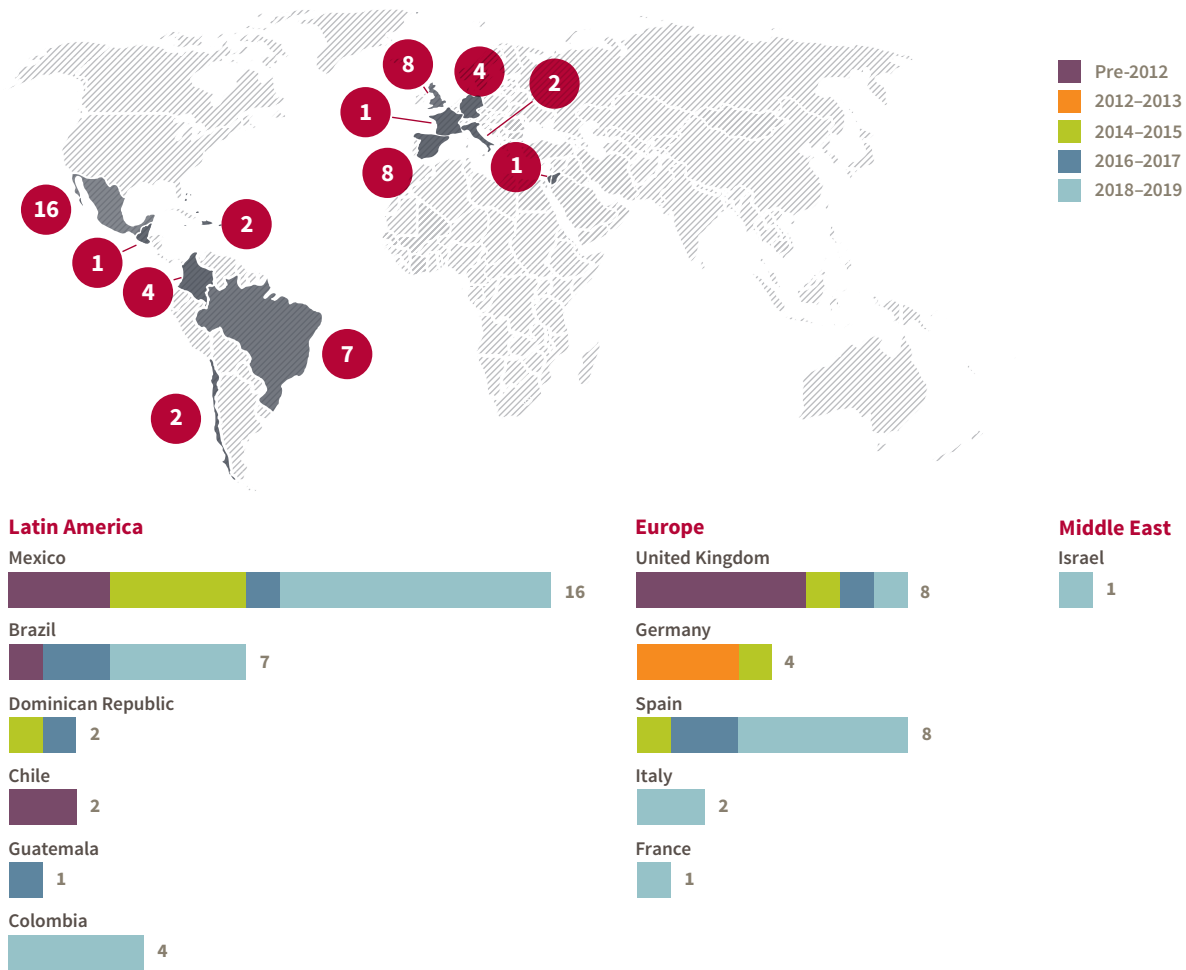
The 2020 IESE Search Fund Study identified 132 first-time international search funds as of December 31, 2019. Fifty funds, or 32% of all international funds identified, were raised in 2018 and 2019. In the last two years, continental Europe and Latin America (excluding Mexico) saw the highest growth, with 24 and 12 new search funds launched, respectively. Additionally, the first search funds in Australia and Japan were started in the 2018 and 2019 period.

As of December 31, 2019, there were 50 search funds seeking to acquire a company. In the 2018 and 2019 period there were 26 acquisitions, bringing the total number of acquired companies outside the United States and Canada to 56. Of the 56 completed acquisitions, nine were sold with positive returns, four had exited with loss of equity, and 43 were still operating (see **Figure O**).

¹⁴ Based on geographic regions as defined by the United States and Canadian censuses. “State” is also used to refer to Canadian provinces here for the sake of simplicity.

¹⁵ International Search Funds—2020: Selected Observations (available at: <https://media.iese.edu/research/pdfs/ST-0603-E.pdf>)

FIGURE O | INTERNATIONAL SEARCH FUND ACQUISITIONS, BY REGION, COUNTRY, AND YEAR



Source: Data from IESE search fund surveys.

International search funds have achieved an ROI of 2.4x and an IRR of 28.7%. The median fund returned 1.1x initial search fund investors’ capital, whereas the top-performing fund returned 23.4x. The aggregate international search fund ROI increased from 2.3x in 2018 to 2.4x in 2020. This reflected a shorter average hold time due in part to the greater number of recent acquisitions that have not reached an exit (sale, recap, etc.). Further detail and analysis of international search funds can be found in [IESE’s International Search Funds—2020: Selected Observations](#).

Alternative Search Fund Models

As awareness of the search fund model has grown over the years, different approaches have emerged and achieved increasing popularity. Self-funded, single-investor, accelerator, and Entrepreneur in Residence (EIR) models have all grown along with the traditional funded model addressed in this study. Recently we have seen an increase in newer search models, such as search-to-start and long-term hold. Each approach has advantages and disadvantages, as does the traditional funded approach to search. Stanford GSB has not collected sufficient data on companies acquired through these other models to report on them yet, but the growing cohorts of entrepreneurs and companies acquired through these interesting alternative models warrant examination. Further discussion of these models can be found in **Appendix C**.

Conclusion

The search fund community continues to grow, thrive, and change. The last two years saw records in the number of search funds launched, acquisitions made, and successful exits. Acquisition multiples have remained consistent, and returns have decreased but continue to exceed 30% IRR. Over time search strategies have evolved, with more following a deep-dive approach and increased interest in Healthcare and Software. We anticipate that the model will continue evolving and look forward to reporting on it in future studies.

Acknowledgements

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EXHIBIT 1 | CHARACTERISTICS OF SEARCH FUND PRINCIPALS¹⁶

| | PRE-2001 | 2002-2003 | 2004-2005 | 2006-2007 | 2008-2009 | 2010-2011 | 2012-2013 | 2014-2015 | 2016-2017 | 2018-2019 |
|--|----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
|--|----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|

Age at Start of Search

| | | | | | | | | | | |
|----------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| MINIMUM | 26 | 28 | 28 | 27 | 26 | 25 | 24 | 24 | 26 | 25 |
| MEDIAN | 30 | 31 | 32 | 32 | 30 | 30 | 30 | 32 | 32 | 32 |
| MAXIMUM | 35 | 60 | 47 | 50 | 51 | 51 | 46 | 54 | 47 | 55 |
| UNDER 30 | N/A | 12% | 30% | 33% | 35% | 39% | 49% | 25% | 26% | 21% |
| 30-35 | N/A | 65% | 53% | 47% | 40% | 31% | 36% | 49% | 39% | 56% |
| 36-40 | N/A | 12% | 10% | 10% | 16% | 14% | 11% | 20% | 32% | 17% |
| OVER 40 | N/A | 12% | 7% | 10% | 9% | 17% | 4% | 7% | 3% | 6% |

Number of Post-MBA Years Before Search Fund

| | | | | | | | | | | |
|-----------------------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| MINIMUM ¹⁷ | N/A | 0 | 0 | 0 | 0 | 0 | -1 | -1 | -2 | 0 |
| MEDIAN | N/A | 2 | 1 | 1 | 4 | 2 | 0 | 1 | 3 | 1 |
| MAXIMUM | N/A | 10 | 18 | 16 | 20 | 17 | 10 | 26 | 15 | 18 |
| NO MBA | N/A | N/A | 0% | 13% | 16% | 14% | 20% | 18% | 19% | 16% |
| <1 YEAR POST-MBA | N/A | N/A | 47% | 33% | 18% | 42% | 49% | 35% | 25% | 28% |
| 1-3 YEARS POST-MBA | N/A | N/A | 17% | 27% | 20% | 17% | 20% | 24% | 19% | 34% |
| 4-7 YEARS POST-MBA | N/A | N/A | 23% | 20% | 22% | 17% | 7% | 12% | 21% | 13% |
| >7 YEARS POST-MBA | N/A | N/A | 13% | 7% | 24% | 11% | 4% | 10% | 16% | 9% |

Gender

| | | | | | | | | | | |
|--------|-----|------|------|------|------|-----|------|-----|-----|-----|
| MALE | 96% | 100% | 100% | 100% | 100% | 94% | 100% | 95% | 92% | 93% |
| FEMALE | 4% | 0% | 0% | 0% | 0% | 6% | 0% | 5% | 8% | 7% |

Source: Data from Stanford GSB search fund surveys.

¹⁶ Totals may not sum to 100% due to rounding.

¹⁷ Negative numbers in the "minimum" row reflect a small number of searchers who raised searched capital and started searching before graduating from business school.

EXHIBIT 2 | SEARCH FUND PRINCIPALS' PROFESSIONAL BACKGROUNDS¹⁸

| PROFESSIONAL BACKGROUND | 1984–2001 | 2002–2003 | 2004–2005 | 2006–2007 | 2008–2009 | 2010–2011 | 2012–2013 | 2014–2015 | 2016–2017 | 2018–2019 |
|--------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|------------------|
| MANAGEMENT CONSULTING | 26% | 23% | 10% | 26% | 7% | 14% | 16% | 11% | 7% | 12% |
| INVESTMENT BANKING/ FINANCE | 23% | 10% | 16% | 27% | 20% | 11% | 22% | 11% | 16% | 22% |
| SALES | 12% | 1% | 3% | 7% | 4% | 6% | 4% | 6% | 3% | 8% |
| VENTURE CAPITAL | 8% | 3% | 5% | 1% | 0% | 0% | 2% | 0% | 3% | 0% |
| LINE/GENERAL MANAGEMENT | 5% | 27% | 7% | 15% | 11% | 19% | 2% | 12% | 14% | 17% |
| MARKETING | 5% | 2% | 4% | 0% | 4% | 0% | 0% | 0% | 1% | 2% |
| LAW | 4% | 0% | 2% | 0% | 0% | 0% | 7% | 3% | 0% | 0% |
| OPERATIONS | 4% | 7% | 16% | 1% | 7% | 8% | 7% | 5% | 23% | 3% ¹⁹ |
| ENTREPRENEUR | 2% | 13% | 8% | 7% | 13% | 6% | 4% | 3% | 4% | 8% |
| ACCOUNTING | 2% | 0% | 3% | 0% | 0% | 0% | 0% | 2% | 1% | 1% |
| ENGINEERING | 2% | 0% | 5% | 2% | 0% | 6% | 2% | 1% | 4% | 7% |
| MILITARY | 2% | 1% | 8% | 1% | 0% | 0% | 2% | 9% | 3% | 5% |
| INSURANCE | 2% | 1% | 0% | 2% | 0% | 0% | 0% | 0% | 0% | 0% |
| PRIVATE EQUITY | 1% | 5% | 11% | 4% | 27% | 28% | 31% | 27% | 14% | 14% |
| OTHER | 0% | 7% | 2% | 8% | 7% | 3% | 0% | 11% | 7% | 1% |

Source: Data from Stanford GSB search fund surveys.

¹⁸ Totals may not sum to 100% due to rounding.

¹⁹ We refined the professional background categories for the 2018 study, complicating comparisons with categories from previous studies. In 2018, we changed “Operations” to “Operating Management,” and then in 2020 changed it back because of confusion with the term, thus contributing to the volatility in reported Operations backgrounds.

EXHIBIT 3 | COMPARISON OF SEARCH FUND METRICS

| | PRE-2001 | 2002-2003 | 2004-2005 | 2006-2007 | 2008-2009 | 2010-2011 | 2012-2013 | 2014-2015 | 2016-2017 | 2018-2019 |
|--|----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
|--|----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|

Number of Principals

| | | | | | | | | | | |
|----------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| SINGLE | 68% | 41% | 42% | 75% | 36% | 62% | 59% | 72% | 55% | 80% |
| PARTNERS | 32% | 59% | 58% | 25% | 64% | 38% | 41% | 28% | 45% | 20% |

Amount of Initial Capital Raised

| | | | | | | | | | | |
|---------|-------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| MINIMUM | \$40,000 | \$125,000 | \$150,000 | \$200,000 | \$200,000 | \$140,000 | \$125,000 | \$175,000 | \$250,000 | \$300,000 |
| MEDIAN | \$290,000 | \$350,000 | \$395,000 | \$385,000 | \$450,000 | \$446,250 | \$426,000 | \$420,000 | \$450,000 | \$450,000 |
| MAXIMUM | \$1,000,000 | N/A | \$750,000 | \$550,000 | \$750,000 | \$850,000 | \$650,000 | \$722,000 | \$825,000 | \$900,000 |

Amount of Initial Capital Raised per Principal

| | | | | | | | | | | |
|---------|-----|-----|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| MINIMUM | N/A | N/A | \$106,250 | \$175,000 | \$143,750 | \$140,000 | \$125,000 | \$175,000 | \$150,000 | \$235,000 |
| MEDIAN | N/A | N/A | \$276,250 | \$350,000 | \$262,500 | \$302,500 | \$355,000 | \$385,000 | \$398,000 | \$429,000 |
| MAXIMUM | N/A | N/A | \$750,000 | \$540,000 | \$450,000 | \$575,000 | \$560,000 | \$640,000 | \$600,000 | \$570,000 |

Number of Search Fund Investors

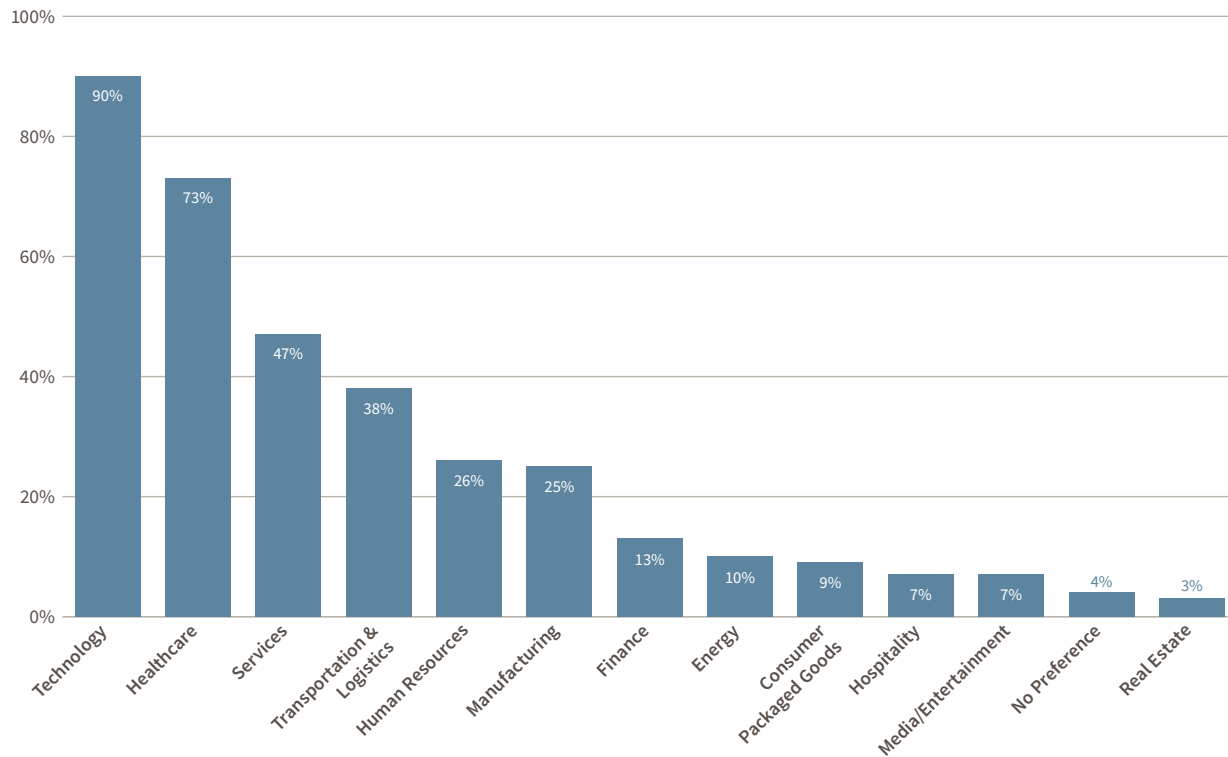
| | | | | | | | | | | |
|---------|----|----|----|----|----|------|----|------|----|----|
| MINIMUM | 2 | 1 | 3 | 10 | 5 | 8 | 2 | 5 | 2 | 3 |
| MEDIAN | 12 | 13 | 12 | 14 | 15 | 18.5 | 16 | 15.5 | 15 | 15 |
| MAXIMUM | 25 | 20 | 24 | 23 | 28 | 26 | 30 | 25 | 24 | 27 |

Number of Months Fundraising

| | | | | | | | | | | |
|---------|-----|-----|------|------|------|------|-----|-----|------|------|
| MINIMUM | N/A | 1.0 | 2.0 | 0.8 | 0.0 | 1.5 | 0.8 | 0.0 | 1.0 | 0.0 |
| MEDIAN | N/A | 4.5 | 5.0 | 3.0 | 4.0 | 3.8 | 4.1 | 3.0 | 3.0 | 3.1 |
| MAXIMUM | N/A | 9.0 | 12.0 | 10.0 | 20.0 | 28.4 | 8.6 | 8.0 | 11.0 | 12.2 |

Source: Data from Stanford GSB search fund surveys.

EXHIBIT 4A | TARGETED INDUSTRIES, 2018–2019 (N = 89)²⁰



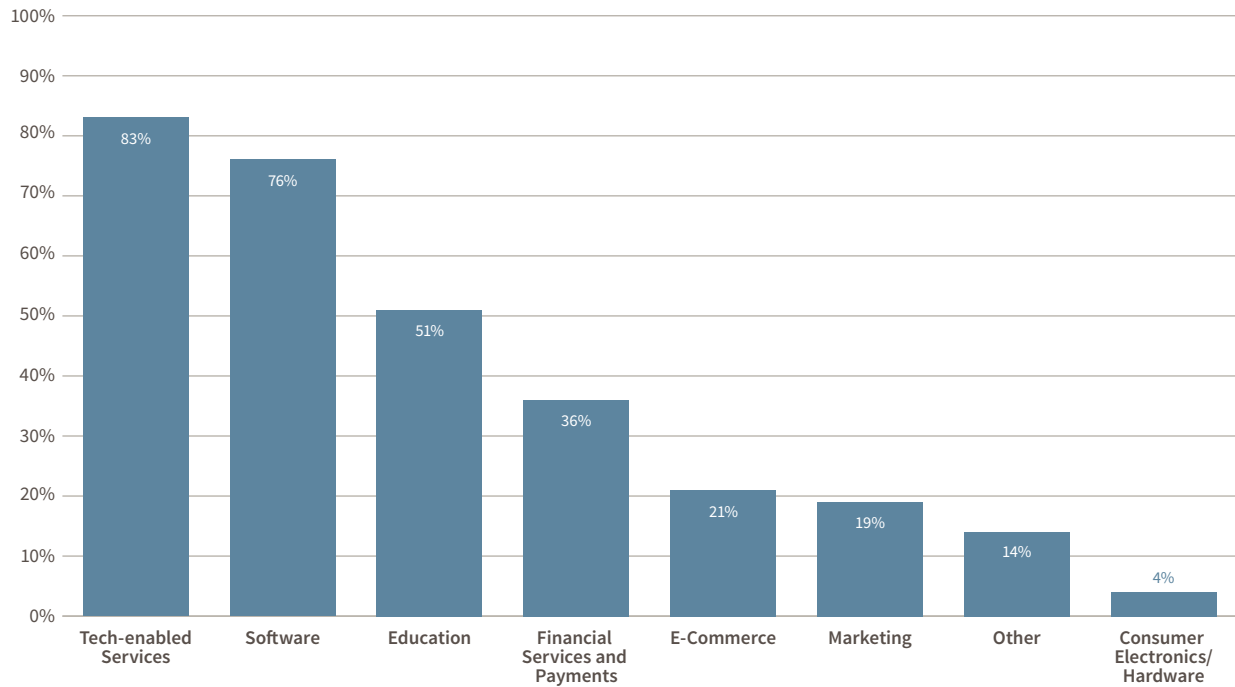
Source: Data from Stanford GSB search fund surveys.

For historical data on industries targeted by searchers (Pre-2001–2015), please refer to previous versions of the *Search Fund Study*.²¹

20 Starting in 2016, principals had the option to select all industries they targeted in their search rather than choosing only one. The above data represent the frequency of each response across all search funds newly surveyed for these years. Additionally, the “Internet or IT” category was redefined as “Technology” in the 2016 study and broken into subcategories for the 2018 and 2020 studies, as shown in Exhibit 4B. “Healthcare” as defined in the 2016 study is broken down into subcategories for 2018 and 2020, as shown in Exhibit 4C.

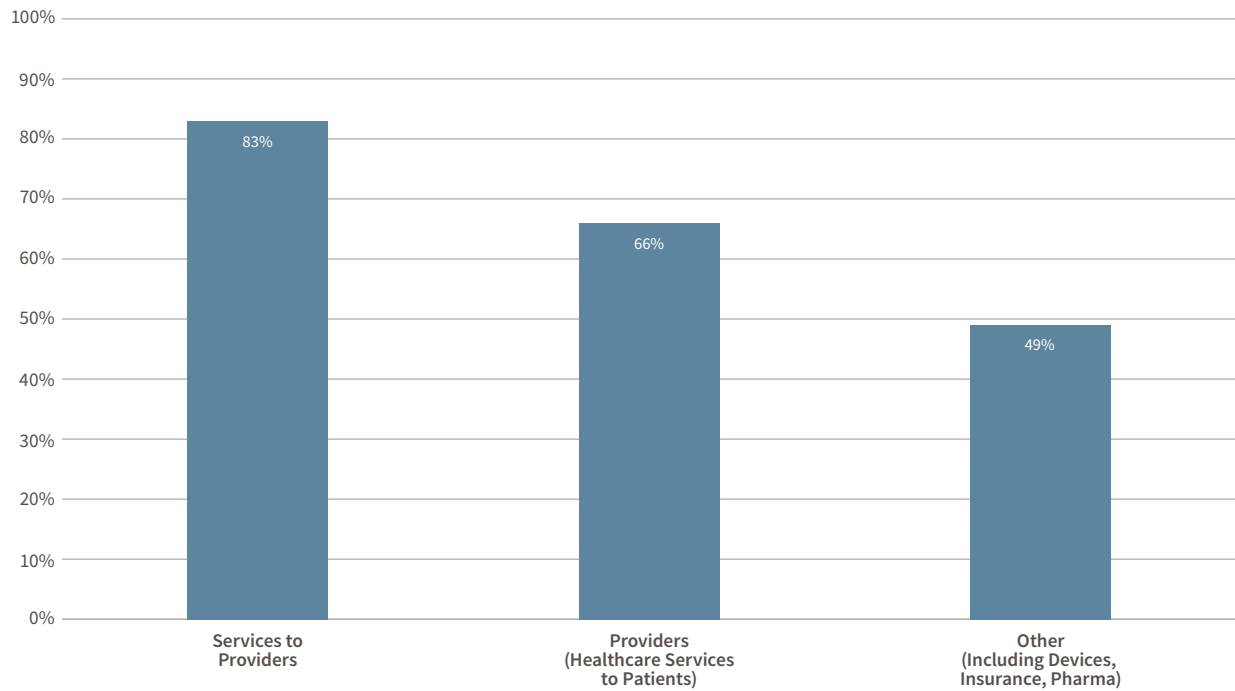
21 Previous versions of the Search Fund Study are available at: <https://www.gsb.stanford.edu/faculty-research/centers-initiatives/ces/research/search-funds>.

EXHIBIT 4B | TARGETED TECHNOLOGY SUBCATEGORIES, 2018–2019 (N = 80)



Source: Data from Stanford GSB search fund surveys.

EXHIBIT 4C | TARGETED HEALTHCARE SUBCATEGORIES, 2018–2019 (N = 65)



Source: Data from Stanford GSB search fund surveys.

EXHIBIT 5 | MEDIAN STATISTICS FOR RECENT SEARCH FUND ACQUISITIONS

| MEDIAN | ALL ACQUISITIONS | 2006-2007 | 2008-2009 | 2010-2011 | 2012-2013 | 2014-2015 | 2016-2017 | 2018-2019 |
|-----------------------------------|------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| LENGTH OF SEARCH (MONTHS) | 21 | 19 | 14 | 18 | 19 | 17 | 23 | 23 |
| PURCHASE PRICE | \$10.8 M | \$9.4 M | \$6.5 M | \$7.9 M | \$11.6 M | \$12.0 M | \$13.1 M | \$10.0 M |
| COMPANY REVENUES AT PURCHASE | \$8.0 M | \$9.1 M | \$5.3 M | \$6.0 M | \$6.2 M | \$7.0 M | \$10.0 M | \$6.3 M |
| COMPANY EBITDA AT PURCHASE | \$2.0 M | \$2.0 M | \$1.3 M | \$1.5 M | \$2.0 M | \$2.5 M | \$2.1 M | \$1.8 M |
| COMPANY EBITDA MARGIN AT PURCHASE | 21.7% | 18.2% | 20.5% | 23.5% | 29.9% | 23.4% | 22.7% | 21.0% |
| EBITDA GROWTH RATE AT PURCHASE | 17.5% | 16.5% | 9.3% | 11.9% | 18.0% | 5.0% | 20.0% | 15.0% |
| PURCHASE PRICE/EBITDA | 6.0x | 5.2x | 4.9x | 5.2x | 5.6x | 5.8x | 6.3x | 6.0x |
| PURCHASE PRICE/REVENUE | 1.5x | 0.9x | 1.5x | 1.3x | 1.6x | 1.5x | 1.1x | 1.4x |
| COMPANY EMPLOYEES AT PURCHASE | 43 | 60 | 38 | 38 | 21 | 46 | 45 | 32 |

Source: Data from Stanford GSB search fund surveys.

EXHIBIT 6 | SELECTED STATISTICS FOR ALL SEARCH FUND ACQUISITIONS²²

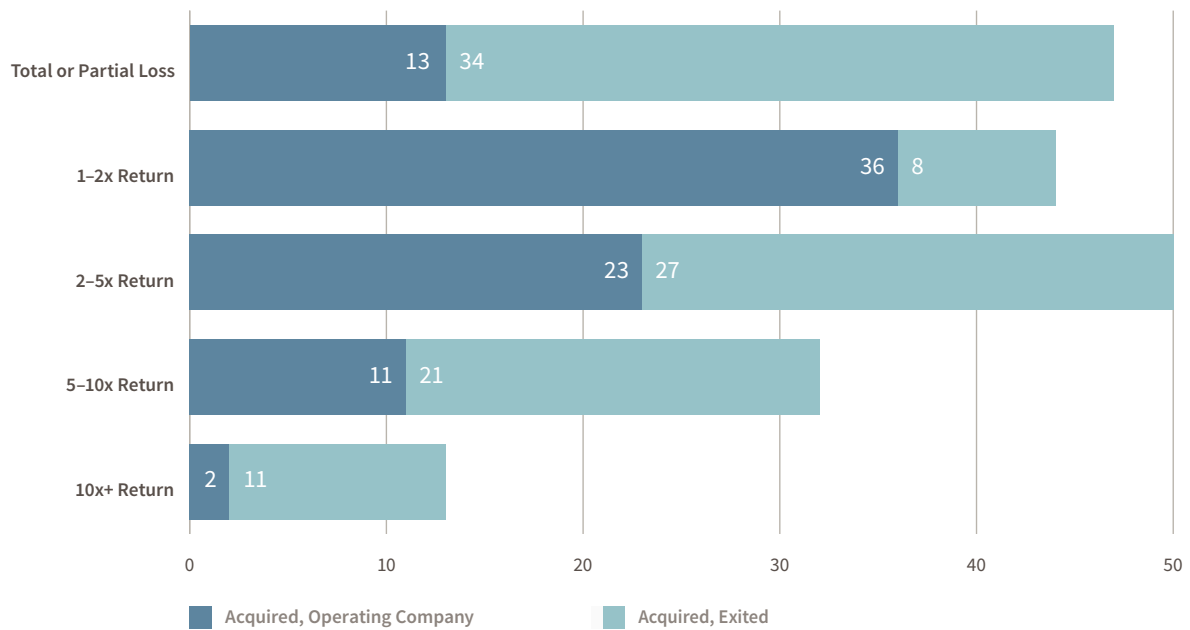
| TOTAL NUMBER OF MONTHS FROM START OF SEARCH TO DEAL CLOSE | | ALL ACQUISITIONS | PURCHASE PRICE STATISTICS | | ALL ACQUISITIONS |
|---|--|------------------|---------------------------|--|------------------|
| MINIMUM | | 2.0 | MINIMUM | | \$1.70 M |
| MEDIAN | | 20.8 | MEDIAN | | \$10.80 M |
| MAXIMUM | | 74.0 | MAXIMUM | | \$117.00 M |
| <11 MONTHS | | 15% | <\$4 M | | 8% |
| 11-20 MONTHS | | 36% | \$4 M TO \$8 M | | 26% |
| 21-30 MONTHS | | 29% | \$8 M TO \$12 M | | 19% |
| 31+ MONTHS | | 20% | \$12 M+ | | 46% |

| ADDITIONAL STATISTICS FOR ALL SEARCH FUND ACQUISITIONS | MINIMUM | MEDIAN | MAXIMUM |
|--|----------|---------|-----------|
| COMPANY REVENUES AT PURCHASE | \$1.2 M | \$8.0 M | \$100.0 M |
| COMPANY EBITDA AT PURCHASE | -\$1.6 M | \$2.0 M | \$25.0 M |
| COMPANY EBITDA MARGIN AT PURCHASE | -18.0% | 21.5% | 57.0% |
| EBITDA GROWTH RATE AT PURCHASE | -56% | 18% | 300% |
| REVENUE GROWTH RATE AT PURCHASE | -20% | 11% | 60% |
| PURCHASE PRICE / EBITDA MULTIPLE | NM | 6.0x | 114.0x |
| PURCHASE PRICE / REVENUE MULTIPLE | 0.1x | 1.5x | 7.7x |
| COMPANY EMPLOYEES AT PURCHASE | 4 | 43 | 740 |

Source: Data from Stanford GSB search fund surveys.

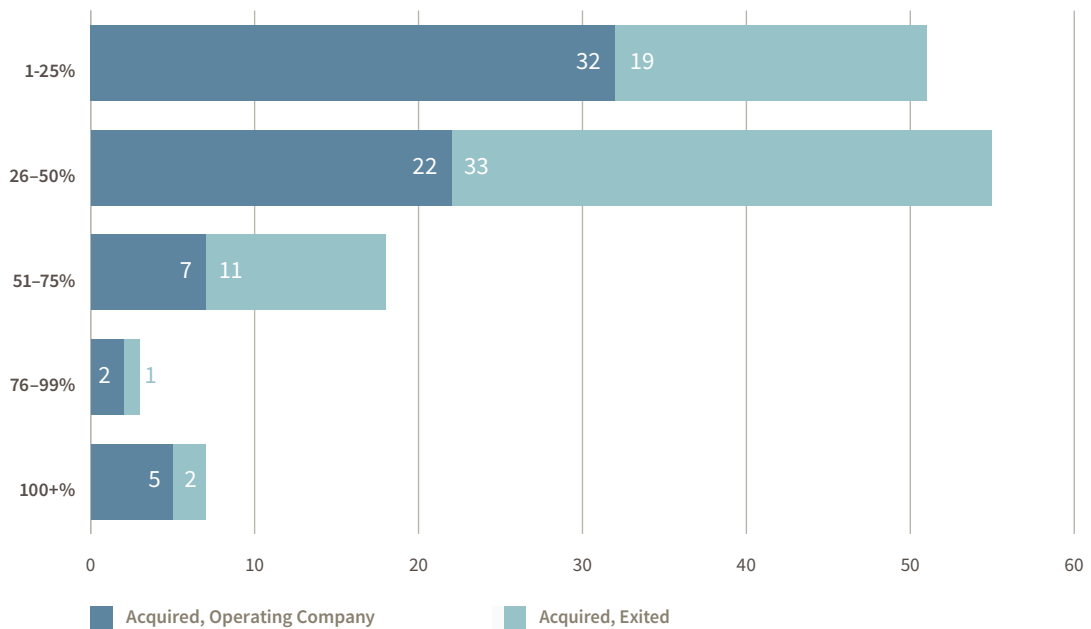
²² Data on some older acquisitions is incomplete, requiring their exclusion from some calculations and resulting in different sample sizes.

EXHIBIT 7 | ROI DISTRIBUTION OF SEARCH-ACQUIRED COMPANIES (N = 186)²³



Source: Data from Stanford GSB search fund surveys.

EXHIBIT 8 | IRR DISTRIBUTION OF SEARCH-ACQUIRED COMPANIES (N = 134)²⁴



Source: Data from Stanford GSB search fund surveys.

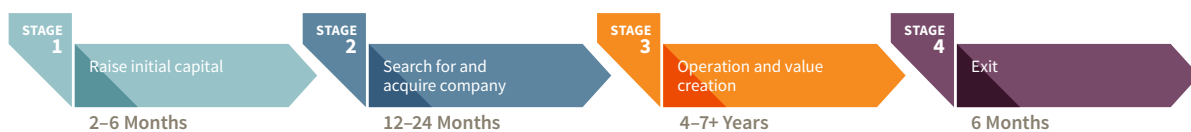
23 Of the 204 companies acquired as of December 31, 2019, for which we have data or collected data historically, 18 funds had been operating for less than one year. Thus, ROI data was calculated for 186 funds.

24 Of the 186 companies for which we could calculate returns as of December 31, 2019, 134 reported positive IRRs as of December 31, 2019.

APPENDIX A | WHAT IS A SEARCH FUND?²⁵

The search fund concept originated in 1984 and has become increasingly well known among business schools and private investors. A search fund is an entrepreneurial path undertaken by one or two individuals (the “searchers”) who form an investment vehicle with a small group of aligned investors, some of whom become mentors, in order for the entrepreneurs to search for, acquire, and lead a privately held company for the medium to long term, typically six to ten years. When successful, this has resulted in a relatively fast path to becoming an owner-CEO, attractive financial returns for both investors and searchers, and growing, well-run enterprises. As shown in the following chart, the search fund process consists of up to four stages: fundraising, search and acquisition, operation, and eventual sale or other event providing shareholder liquidity.

Stages of the Search Fund Lifecycle



The timeframes shown above are estimates for each stage; the time spent on each phase can vary widely.

Stage One: Raise Initial Capital

Search funds are usually structured as limited liability companies. In a search fund, the money is raised in two stages: (1) to fund the search (“search capital”) and (2) to fund the acquisition of a company (“acquisition capital”). The search capital is used to cover a modest salary and administrative and deal-related expenses over a two-year period while the entrepreneur searches full-time for an acquisition. Once a target acquisition is identified and negotiated, the search fund entrepreneur raises the capital to purchase the company.

To formally begin the fundraising process, the searcher composes an Offering Memorandum (also called a Private Placement Memorandum or PPM) to provide to potential investors, presenting the investment opportunity. This document typically includes several sections:

- Executive summary
- Overview of the search fund model
- Outline of the search methodology to be employed, including resources to be utilized
- Potential industries and/or geographies of interest
- Specific criteria to screen acquisition opportunities
- Detailed timeline with expected completion dates for specific activities
- Detailed budget for the uses of the search capital
- Proposal of the form of the investment for the acquisition capital (e.g., subordinated debt and/or equity and the associated coupon/preference)

25 Much of the following content is taken from Mu Y. Li, “Search Funds – 2003, What Has Changed Since 2001.”

- Financial model showing potential investment returns under various scenarios of an illustrative acquisition
- Outline of the potential exit alternatives
- Summary of the personal backgrounds of the principal (and allocation of future responsibilities if more than one principal)

Aspiring search fund entrepreneurs usually engage experienced legal counsel during fundraising. Qualified legal counsel can help the entrepreneur avoid violating securities laws; assist in creating and documenting the appropriate legal entities for the fund; and help the entrepreneur propose legal, tax, and financial structures to potential investors for the acquisition capital as well as the entrepreneur's earned equity. Searchers are well advised to rely on recent searchers or investors for fundraising and PPM guidance.

Principals today can tap a wide network of potential investors to raise a search fund, including experienced individual and institutional search fund investors, as well as business associates, business owners and executives, and possibly friends and family. Typically, 10 or more investors purchase one or several units of the initial capital of the search fund. These funds will cover the salary and administrative and deal-related expenses (office space, travel, legal fees, certain due diligence fees on deals, etc.) of the search fund for two or more years of searching for a company to acquire and raising acquisition capital. In exchange for the initial search capital, each investor receives (1) the right, but not obligation, to invest pro-rata in the equity required to consummate the acquisition and (2) conversion of the search capital, typically on a stepped-up basis (e.g., 150% of the actual investment), into the securities issued as the acquisition capital.

Most search fund principals solicit investors who also can serve as high-quality advisors. Ideal investors can offer expert guidance and advice in deal evaluation, deal execution, and company management; provide support to the entrepreneur during the ups and downs of the search process; assist in generating deal flow; and provide leverage with lawyers, accountants, and bankers. In many cases, investors are drawn not only to the potential financial returns of a search fund, but also to the psychic benefits of being involved with a young entrepreneur.

Stage Two: Search for and Acquire Company

Compared with raising the initial capital, searching for an acquisition target and completing the transaction is typically more time-consuming, with a median of 23 months. The general economic environment, industry characteristics, sellers' willingness to sell, and regulatory issues are among the factors that can prolong or derail an acquisition process. Depending on the complexity of the deal, it can take three to 12 months or more from the time the opportunity is uncovered until transaction close.

Searchers who focus their search, as well as developing and adhering to a systematic approach of creating deal flow and analyzing deal opportunities, have a higher likelihood of identifying and closing an acquisition.

In order to mitigate operating and investment risks, searchers generally target industries that are not subject to rapid technological change, are fairly easy for them to understand, and are in fragmented geographical or product markets. Within the preferred industries, companies are targeted based on their sustainable market position, their history of positive, stable cash flows, and opportunities for improvement and growth. Searchers and their investors tend to prefer healthy, profitable companies over turnaround situations. Adhering to a disciplined list of acquisition guidelines reduces some of the risk of investing in a company run by entrepreneurs who often possess little operating experience.

When a target is identified, the searcher must simultaneously undertake several efforts:

- Negotiate the company purchase with the seller(s)
- Perform due diligence on the company
- Arrange for the senior debt and subordinated debt from third parties (if any)
- Negotiate the structure of the acquisition capital and secure commitments from the original search fund investors
- Secure additional equity commitments if needed
- Finalize the searcher's earned equity allocation and performance targets with the investor base
- Plan the transition for when the acquisition closes and the entrepreneur assumes management of the company

In addition to the follow-on equity investment from the original group of investors, the funds for the acquisition can come from a combination of other sources: seller debt, seller equity rollover, earnouts, traditional senior and subordinated loans, and equity financing from new investors. The capital structure, and therefore equity requirement, can vary widely by industry and the current lending environment.

The acquisition is expected to be at fair market value. Ideally, the acquired company would provide adequate cash flow and not be highly leveraged, so that the short-term survival of the company does not rely on immediate, significant improvement in company performance.

If the initial search capital is exhausted before an acquisition is completed, the searcher may choose either to close the fund or to solicit additional funding to continue the search.

Stage Three: Operation and Value Creation

Upon completing the acquisition, the searcher will establish a board of directors for the company, which often includes substantial representation from the investor base. In the first six to 18 months after the acquisition, searchers typically make few significant changes to the existing business, opting instead to gain familiarity with its inner workings and finer details. After becoming comfortable operating the business, searchers then make changes as they see fit. Searchers can create value through revenue growth, improvements in operating efficiency, appropriate use of leverage, organic expansion, add-on acquisitions, or multiple expansions. These means of creating value are not mutually exclusive; ideally, more than one will apply to a search fund investment. When a growth plan is executed successfully, the searcher shares in the increase in equity value through personal earned equity.

Stage Four: Exit

Most search funds are established with a long-term outlook, generally greater than a five-year time horizon and often longer. Even so, investors and principals share a desire to realize returns at some point; consequently, principals evaluate exit alternatives throughout the life of the business. Liquidity events for investors and principals can occur in a number of ways: Companies can be sold or taken public; investor debt may be repaid; investor equity may be sold to other investors or bought by the company; or the company can issue dividends.

APPENDIX B | FINANCIAL RETURN METHOD

This study calculated financial returns from the perspective of initial search investors. That is, it measured returns based on investments from and distributions to the original search fund investors who invested in both the *search* and *acquisition* phases of the deal. As in the 2018 study, this year's study excluded follow-on financing events.²⁶ This study uses two measures of return: ROI²⁷ and IRR.²⁸ Both ROI and IRR were calculated on a cash flow basis, including both equity and investor debt that was invested as initial search capital and as acquisition capital. These include the losses from searches that ended without an acquisition, losses in equity upon exit, and losses in equity value reported while operating the company.

All returns were calculated on a pre-tax basis using data provided by the principals of the funds or, in the few instances when they were not reachable, by their fund investors. Returns were calculated using the actual investments into each fund and the subsequent acquisitions, when they were made, and eventual distributions. In this study, we conducted an independent audit of calculation methods and checked returns information collected through our survey against data provided by investors, where possible.

26 While follow-on financings can be an important part of search fund returns, excluding them in these calculations simplifies data reporting for searchers, thereby increasing data integrity and accuracy, while staying true to the focus on returns for original search and acquisition investors.

27 Return on investment (ROI) represents the multiple of initial capital invested that is returned to investors (also known as multiple of invested capital or MOIC) — i.e., if the group of initial investors invested \$5 million and received back \$10 million, this would be described as a 2.0x ROI. A return of \$1 million would be a 0.2x ROI and so forth. A complete loss of capital is an ROI of 0.0x.

28 Internal rate of return (IRR) represents the annual compounding rate derived from the actual amounts of search and acquisition capital invested and returned by an investment. For investments returning only a fraction or none of an investment, IRR is not a meaningful metric.

APPENDIX C | ALTERNATIVE SEARCH FUND MODELS

Self-Funded Search

Self-funded searchers do not raise search capital from others and instead fund their own search costs, often living frugally, over similar search periods as traditional searches (up to three years). They maintain an informal network of mentors and investors who help them screen possible deals and work to bring this group of investors together formally at the point of acquiring a company. Self-funded searchers typically rely on raising more debt to complete an acquisition and often target materially smaller companies than funded searchers. As a result, self-funded searchers typically wind up with higher percentage equity ownership (50–70%) of a smaller company than funded searchers. They also often have a smaller set of investor-advisors and a different set of general management and leadership opportunities. The self-funded model may give searchers increased flexibility, notably in the location, industry, type, and size of business they target for acquisition.

Single-Investor, Accelerator, or EIR Model

In the single-investor or “captive” model, searchers are funded by a single investor, either a firm or occasionally a person, and receive a salary, advice, support, and access to networks from that sole investor. This may be a private equity firm, family office, single professional investor, or “accelerator.” Some, especially accelerators, provide common services to the searchers, which might include training, database access, shared interns, mentoring, bank introductions, and prearranged legal and accounting relationships. Economics for the searcher are generally similar to the funded model.



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