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Search Funds vs. Private Equity: The Drivers of Outperformance

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Abstract

This thesis investigates the drivers of performance in Search Fund (SF) acquisitions compared to Private Equity (PE) investments in European small and medium-sized enterprises (SMEs). Search Funds represent a distinctive model of Entrepreneurship Through Acquisition (ETA), whereby an entrepreneur raises capital to identify, acquire, and manage a single privately held company. While SFs have historically delivered aggregate returns that often exceed those of PE, it remains unclear whether this outperformance is driven by superior managerial execution after acquisition or by rigorous pre-acquisition target selection.

The research is motivated by the strategic importance of SMEs in Europe, where they account for more than 99% of enterprises and face a looming succession crisis due to aging ownership and limited family successors. In this context, SFs may play a critical role in ensuring continuity, preserving jobs, and fostering entrepreneurial ownership. Yet empirical evidence on their performance in Europe remains limited, with most existing studies focused on North America and relying on descriptive or survey-based data.

To address this gap, the study builds a panel dataset of European SME acquisitions between 2014 and 2021, including 27 SF-backed and 745 PE-backed firms. Using firm-level financial data from Orbis, AIDA, and Refinitiv, the analysis applies Ordinary Least Squares regressions and Difference-in-Differences estimators to compare pre- and post-acquisition dynamics across ownership models. Performance is assessed through firm-level financial indicators capturing profitability, efficiency, growth, and leverage.

The findings strongly support the hypothesis that SFs outperform primarily due to disciplined target selection. SF-backed companies display significantly higher financial strength before acquisition, but they do not improve more than PE-backed firms after the deal. This indicates that the relative advantage of SFs originates from the quality of the firms they acquire rather than from post-acquisition managerial transformation.

The contribution of this study is twofold. Academically, it provides one of the first systematic, data-driven comparisons between SFs and PE in Europe. Practically, it highlights the importance of the rigorous investment criteria applied by searchers in sourcing and evaluating targets, which emerge as the key determinant of long-term outcomes.

Introduction

This thesis investigates the sources of performance differentials between Search Fund (SF) and Private Equity (PE) acquisitions, with a specific focus on the European SME context. The choice of this topic is motivated by both academic and practical considerations. From an academic perspective, it reflects the growing relevance of Entrepreneurship Through Acquisition (ETA) in contemporary entrepreneurial finance, a field that has increasingly attracted the attention of scholars and practitioners. From a practical standpoint, it is directly connected to my professional experience within an Italian Search Fund, which has provided first-hand exposure to the dynamics of this investment vehicle. This dual perspective allows for the integration of rigorous theoretical and empirical analysis with insights derived from practice, thereby reinforcing the significance of the research.

Over the past decades, entrepreneurial finance has expanded well beyond the traditional dichotomy of start-ups and private equity, giving rise to innovative models that combine entrepreneurship with acquisition strategies. ETA represents one of the most notable of these frameworks, enabling individuals to become business owners not by founding new ventures but by acquiring existing firms. Within this broader context, Search Funds have emerged as a particularly distinctive model: one or two entrepreneurs raise capital from a group of investors with the purpose of identifying, acquiring, and subsequently managing a privately held company. Originating in the United States in the 1980s, SFs have since spread internationally and have become increasingly relevant in Europe, where demographic pressures and succession challenges are reshaping the landscape of small and medium-sized enterprises (SMEs).

The distinctiveness of the Search Fund model lies in its positioning between traditional entrepreneurship and private equity. Unlike private equity funds, which are built around professional investment teams, diversified portfolios, and financial engineering, Search Funds rely on the leadership of a single entrepreneur who dedicates his or her efforts to a single acquisition. The two models also address agency problems differently: whereas PE relies on mechanisms such as carried interest and delegated monitoring, SFs achieve alignment through progressive vesting of the searcher's equity and through the close, hands-on involvement of investors (Johnson, 2014; Morrissette, 2015; Simon, 2021). Furthermore, SFs generally employ lower leverage and adopt longer holding periods than PE, shaping not only their risk–return profile but also their approach to value creation.

The economic and social implications of this phenomenon are substantial. SMEs form the backbone of the European economy: they account for more than 99% of all firms, employ approximately 60–65% of the workforce, and generate just over half of total value added (Eurostat, 2023). Yet many of them face a looming

succession crisis. The aging of business owners and the absence of heirs willing or able to continue the family enterprise threaten the continuity of thousands of companies. This challenge is systemic: failure to address it could undermine employment, local development, and industrial competitiveness across the continent. Within this context, Search Funds provide a pragmatic solution by ensuring continuity, safeguarding jobs, and professionalizing management. At the same time, the model gives investors access to an underserved segment of the private equity market and offers entrepreneurs the opportunity to assume CEO roles at an early stage in their careers.

Despite their growing relevance, important questions remain unanswered. Chief among these is the explanation for the superior aggregate returns historically reported by SFs compared to PE. Are such outcomes primarily the result of post-acquisition managerial excellence—linked to the entrepreneur taking over as CEO—or do they stem from disciplined ex-ante target selection? This causal distinction is central to understanding the true nature of value creation in the SF model. Yet the empirical literature, still limited and largely concentrated on North America, has not provided a conclusive answer. Most existing contributions rely on descriptive surveys, case studies, or anecdotal evidence, leaving ample room for more systematic and quantitative investigations.

Although research on Search Funds has expanded considerably in recent years, several gaps remain. The most comprehensive studies, such as those by Stanford GSB and IESE Business School, have focused primarily on the United States and Canada, where the model originated and matured. Systematic, quantitative evidence on European cases remains scarce, despite the growing adoption of SFs across the continent. Moreover, the mechanisms underpinning Search Fund outperformance remain ambiguous. While aggregate returns are consistently reported as attractive, prior research has not determined conclusively whether these results reflect superior post-acquisition management or the rigorous pre-acquisition selection of resilient targets. Few studies explicitly compare SFs with PE, even though the two models often operate within the same SME segment. The absence of such comparisons is notable, given that PE continues to dominate private investment in SMEs, while SFs concentrate on single deals with a higher degree of investor involvement.

This study seeks to fill these gaps by conducting an empirical analysis of SF and PE acquisitions in Europe between 2014 and 2021. The European focus is motivated by several considerations. First, the Search Fund ecosystem in Europe is relatively young and less mature than in North America, making it especially relevant for analysis. Second, the regional scope ensures greater consistency in legal, institutional, and accounting frameworks, while taking advantage of the comparatively broader availability of standardized SME financial data in Europe. Third, the European context is highly relevant for policy debates, given the scale of the succession challenge and the critical role of SMEs in sustaining economic growth, innovation, and employment.

The scope of the analysis is deliberately bounded. Only small and medium-sized enterprises with revenues below €60 million are included, as this range reflects the natural domain of Search Fund targets as well as the overlapping segment of mid-market PE. This choice enhances comparability between the two ownership models. The temporal scope, limited to the years 2014–2021, provides a sufficiently recent and consistent window while also ensuring an adequate number of observations. Moreover, the analysis relies on firm-level financial data rather than deal-level transaction data, since reliable information on private transaction structures is scarce. This methodological choice ensures consistency across both groups and allows for a clearer identification of performance trends.

Methodologically, the thesis employs a firm-year panel dataset comprising 4,632 observations, of which 162 are from SF-backed firms and 4,470 from PE-backed firms. Data were collected from Orbis, Orbis M&A, AIDA, and Refinitiv, and standardized in nominal euros. The empirical strategy combines Ordinary Least Squares regressions with Difference-in-Differences estimators to disentangle the effects of ex-ante selection from those of post-deal management. Firm performance is evaluated through standard financial indicators, including profitability, efficiency, growth, and leverage.

The empirical investigation is structured around three hypotheses. H1 tests whether SF-backed firms already display superior financial performance prior to acquisition compared to PE-backed firms. H2 examines whether SF-backed firms improve more than PE-backed firms after the acquisition. H3 integrates the results to assess whether the source of outperformance lies in disciplined selection rather than operational execution.

The contribution of this work is twofold. From an academic perspective, it adds to the literature on entrepreneurial finance by offering one of the first systematic, data-driven comparisons between SF and PE acquisitions in Europe. From a practical perspective, it provides insights for investors, entrepreneurs, and policymakers on the circumstances under which SFs can serve as an effective vehicle for succession, value creation, and sustainable growth in the SME segment. By clarifying whether superior outcomes stem from managerial action or from target selection, the study also informs broader debates on how to design policies and investment strategies that support SME continuity in the face of demographic and economic challenges.

The structure of the thesis reflects this progression from theoretical foundations to empirical evidence and interpretation. Chapter 1 introduces the conceptual basis of ETA and traces the evolution of the Search Fund model. Chapter 2 examines the strategic, economic, and geographical dimensions of SFs, with particular emphasis on their diffusion in Europe and their comparison with PE. Chapter 3 sets out the dataset, methodological approach, and research hypotheses. Chapter 4 presents the empirical results and interprets them in light of the hypotheses. Finally, Chapter 5 discusses the strategic implications of the findings, highlights the study's limitations, and outlines directions for future research.

Chapter 1- Theoretical Framework: Entrepreneurship Through Acquisition

1.1 Entrepreneurship Through Acquisition: Key Concepts and Economic Context

1.1.1 Definition and Core Principles

Entrepreneurship Through Acquisition (ETA) is a path to entrepreneurship that involves acquiring and directly managing an existing business, often through a leveraged management buy-in. Unlike traditional startups—built from the ground up—ETA focuses on companies that already have an established market position, customer base, and operational infrastructure. The aim is to take a solid business and professionalize, grow, and scale it further (Hunt & Fund, 2012).

Entrepreneurs who pursue this model are typically MBA graduates or experienced professionals who combine their managerial skills with external capital to acquire and lead a company (Dennis & Laseca, 2016). As outlined by Kelly et al. (1986), ETA transactions rest on three core principles:

1. **Concentrated ownership** – A small group of aligned investors allows for faster and more strategic decision-making.
2. **Majority control** – A lead entrepreneur or investor group holds a controlling stake, ensuring clarity in leadership and direction.
3. **Active managerial involvement** – Unlike passive investment models, ETA entrepreneurs' step into day-to-day leadership roles, focusing on long-term value creation.

These principles distinguish ETA from traditional private equity or purely financial acquisitions, reinforcing its identity as a hands-on, entrepreneurially driven approach.

1.1.2 ETA vs. Traditional Entrepreneurship and Private Equity Buyouts

Entrepreneurship Through Acquisition (ETA) is often mistaken for a form of traditional leveraged buyout (LBO) or private equity (PE) investment. It differs substantially in both intent and execution. While LBOs typically aim to extract value through financial engineering, cost reduction, and relatively short-term gains, ETA focuses on the long-term growth and development of the acquired business (Kelly, 1986).

Unlike traditional forms of entrepreneurial finance—such as venture capital, which funds early-stage startups with uncertain business models and high failure rates—ETA targets established companies with stable revenues, loyal customers, and operational track records. These businesses offer a more predictable platform for sustainable growth, making ETA an appealing alternative for entrepreneurs seeking to reduce startup risk while maintaining full operational engagement (Hunt & Fund, 2012).

One of the clearest distinctions between ETA and private equity lies in leadership. PE firms often retain the existing management team and operate more as strategic overseers. In contrast, ETA entrepreneurs' step in directly, replacing former owners and taking on full operational responsibility (Hunt & Fund, 2012). This hands-on involvement blurs the line between investor and operator, positioning ETA as a hybrid model that combines entrepreneurship, capital deployment, and active business leadership.

1.1.3 Types of ETA Models

As ETA has matured, several models have emerged, each with its own approach to funding and execution (Dennis & Laseca, 2016). These variations offer entrepreneurs different levels of autonomy, financial exposure, and investor involvement. The most common ETA models include:

1. **Traditional Search Fund** – This is the original and most structured model, where one or two entrepreneurs raise capital from a group of investors to support the search, acquisition, and operation of a privately held company. First introduced in 1984, it has since become a recognized asset class with standardized practices and expectations.
2. **Sponsored Search Fund** – A hybrid approach where a single institutional investor, such as a private equity firm or family office, provides the capital in exchange for equity in the target company. The sponsor often brings strategic support and expects a more hands-on relationship than in traditional search funds.
3. **Incubated Searcher** – Similar to a startup accelerator, this model offers structured support including mentorship, funding, and access to networks. The incubator typically covers the financial risk and provides infrastructure, enabling the entrepreneur to focus on executing the acquisition and subsequent management.
4. **Self-Funded Search** – In this model, the entrepreneur personally finances the search phase, foregoing outside capital in exchange for full ownership after the acquisition. While this approach offers greater upside and control, it also exposes the searcher to higher personal financial risk, as all search-related costs are self-borne.
5. **Crowdfunded Search** – A more recent development (introduced around 2016), this model enables searchers to raise capital through online platforms that connect them with a wide base of accredited investors. It offers flexibility but often involves a more complex capital structure, which may include convertible debt, preferred equity, or SAFE notes during the search phase, and customized equity terms at acquisition.

The following table offers a comparative overview of the main Search Fund models, summarizing key dimensions such as flexibility, required infrastructure, investor dynamics, mentorship availability, and potential equity for the searcher. It helps visualize how each model balances autonomy and investor involvement, highlighting the practical trade-offs between financial support and operational independence.

Table 1: Comparison of key Search Fund models by operational structure and economic terms.

	Flexibility / Control	Infrastructure	Investor Base	Mentorship	Potential Equity for Searcher (Solo)
Traditional Search Fund	• Low: monthly reporting to disparate investor base; no committed capital; terms pre-negotiated	• Low: searcher must setup infrastructure individually; limited admin support, if any	• 10-20 investors, each with their own right of first refusal to fund transaction	• Medium: depends on availability of investors; frequency of interaction usually up to the searcher	• 25%
Sponsored Search	• Medium: monthly reporting to in-house investor base; committed capital	• High: office space, IT, admin support, HR and broker/lender relationships in place	• One committed fund; decisions made by investment committee	• Medium-to-high: daily interaction with investor base; incentives aligned; depends on sponsor	• 20 – 30%
Incubated Search	• Medium: monthly reporting to in-house investor base; committed capital	• High: office space, IT, admin support, HR and broker/lender relationships in place	• One committed fund; decisions made by investment committee	• High: daily interaction with investor base with relevant experience; designed to mentor searchers	• 25%
Self-Funded Search	• High: no outside time limits, reporting requirements, or investment mandates	• Low: searcher must setup infrastructure individually; limited admin support, if any	• No pre-determined agreement; terms dependent upon attractiveness and demand	• Low-to-Medium: depends on personal network of searcher; no search capital as incentive to investors	• 30 – 100%
Crowdfunded Search	• Low-to-Medium: reporting depends on investors; disparate investor base; no committed capital	• Low: searcher must setup infrastructure individually; limited admin support, if any	• Varies widely; too early for standard to be developed	• Low-to-Medium: depends on personal network of searcher	• 30 – 100%

Source: Dennis & Laseca (2016)

A brief note on SPACs. Special Purpose Acquisition Companies (SPACs) are sometimes referred to as the public-market equivalent of ETA. While structurally different, they share the logic of raising capital first and then searching for a business to acquire and manage. SPACs are publicly listed entities that raise funds through an IPO with the goal of acquiring a private company. Unlike ETA—where individual entrepreneurs take direct operational control—SPACs are typically managed by investment teams and focus on larger-scale deals. As such, they remain conceptually adjacent but are distinct in scope, governance, and target profile (Simon, 2021).

1.1.4 Economic and Entrepreneurial Context

Entrepreneurship Through Acquisition (ETA) has emerged as a critical solution to the generational transition crisis affecting small and medium-sized enterprises (SMEs). Many of these businesses, particularly those founded by baby boomer entrepreneurs, lack a structured succession plan, which poses significant economic risks if they are not effectively transferred to new owners (Nows, 2021). Research estimates that by 2025,

more than $10 trillion in baby boomer-owned business assets will either be passed down to successors or sold, presenting a unique opportunity for ETA entrepreneurs to take over and revitalize these firms (Lobel, 2008).

ETA's Contribution to Business Continuity and Economic Stability

One of the most significant contributions of Entrepreneurship Through Acquisition (ETA) is its capacity to ensure the continuity of established small and medium-sized enterprises (SMEs), particularly those at risk of closure due to succession failures. Hunt & Fund (2012) estimate that ETA transactions account for approximately 20,000 to 30,000 business acquisitions annually in the United States, contributing between $25 billion and $40 billion in entrepreneurial activity. Many of these acquisitions involve businesses facing stagnation or underperformance, which are subsequently revitalized under new, growth-oriented leadership.

Recent studies further reinforce the urgency and relevance of ETA in addressing a growing global succession crisis. In the United States alone, millions of privately held businesses—representing roughly $4.8 trillion in net worth—are expected to change hands over the next two decades as aging owners retire or pass away, often without clear succession plans (Lindsey et al., 2021). This demographic shift presents a significant economic vulnerability, but also a unique opportunity for a new generation of entrepreneurial operators.

Moreover, the succession gap is not confined to North America. As Nows (2021) highlights, tens of millions of small businesses worldwide lack an identified successor, raising the risk of widespread business discontinuity. In this context, ETA emerges not only as a compelling career path for aspiring entrepreneurs, but also as a vital mechanism to preserve jobs, sustain local economies, and maintain business legacies across generations.

Across Europe, the search fund model is gaining relevance as a potential solution to the growing succession gap among small and medium-sized enterprises (SMEs). According to the latest *Status Report on SME Succession* (2023), an average of 125,000 SME owners will seek to transfer their businesses to a successor each year until at least 2027. While the desire for family succession remains high—57% of owners prefer to pass their business on to a family member—interest among potential successors is declining. As a result, planned successions increasingly fail to materialize.

This mismatch is most visible in the widening gap between succession plans and actual transfers. Each year, only about half as many SME successions are completed as are initiated, primarily due to a lack of interested or qualified successors. This is driving a rise in closure plans, with approximately 97,000 SME owners expected to exit the market without a succession plan by the end of 2024. At the structural level, the share of SME owners considering succession has increased significantly in recent years—from 35% in 2017 to 43% in 2023—driven largely by demographic shifts and accelerated aging among business owners (Kfw Research,2023).

External succession, including ETA transactions, represents a growing share of these transitions. In 2023, 43% of succession planners considered selling their business to an external party, such as a search fund entrepreneur (Kfw Research,2023). These buyers can benefit from acquiring a business with an existing customer base, supplier relationships, experienced staff, and tested operational processes. However, external successions still face greater complexity compared to intra-family transfers, including higher transaction costs, longer timeframes, and greater information asymmetry (Hoffmann,2023).

In this context, ETA offers a pragmatic and entrepreneurial solution. It enables continuity for businesses with no internal successors, while also revitalizing them through professionalized leadership. With succession challenges intensifying across Europe, ETA stands out as a valuable mechanism to preserve economic value and ensure long-term business continuity in the SME sector.

Impact of ETA on Employment and Economic Growth

Beyond ensuring business continuity, ETA also plays a vital role in job retention, local economies, and overall economic dynamism. When incumbent business owners fail to find suitable successors, these companies risk dissolution, leading to negative consequences for employment, innovation, and regional economic stability (Block et al., 2013). However, ETA serves as a mechanism for preserving these businesses, ensuring continued employment for workers and maintaining their contributions to the local economy.

Additionally, ETA transactions foster entrepreneurial dynamism by injecting new leadership, strategic direction, and professionalization into acquired companies. Unlike Traditional Private Equity acquisition, which often emphasize operational continuity, ETA entrepreneurs are incentivized to implement innovation-driven strategies that enhance business performance and competitiveness (Hunt & Fund, 2012). This focus on long-term value creation positions ETA as a unique approach within the broader landscape of business acquisitions.

ETA as an Alternative to Startups

While traditional entrepreneurship literature often emphasizes launching new ventures, Entrepreneurship Through Acquisition (ETA) represents a compelling alternative—particularly for mid-career professionals and MBA graduates. Starting a business from scratch entails substantial risk, with high failure rates linked to poor product-market fit, limited resources, or lack of legitimacy (Hoffmann,2023). In contrast, ETA enables entrepreneurs to acquire existing companies with validated business models, operational infrastructure, and established customer bases—significantly reducing early-stage uncertainty (Xi et al., 2020). This approach is especially relevant today, as millions of privately held businesses are expected to face succession issues in the

coming decades, creating an unprecedented pipeline of acquisition opportunities (Lindsey et al., 2021; Morrissette & Hines, 2015).

Conclusion: ETA's Growing Role in Economic Development

As business ownership transitions become increasingly complex, ETA has emerged as a viable mechanism for addressing succession challenges, preserving economic value, and fostering entrepreneurial growth. With a projected rise in business exits due to aging entrepreneurs, the role of ETA is expected to expand further, shaping the future landscape of small and medium-sized enterprises worldwide. Given its ability to sustain businesses, drive innovation, and safeguard employment, ETA is likely to play an increasingly pivotal role in economic development in the years to come.

1.2 Search Fund: Characteristics and Model

1.2.1 Definition of Search Fund

A search fund is an entrepreneurial journey undertaken by one or two individuals—known as *searchers*—who establish an investment vehicle in collaboration with a small group of aligned investors, some of whom also serve as mentors. The goal is to identify, acquire, and lead a single privately held company over a medium- to long-term horizon, typically ranging from six to ten years. When successful, this model offers a relatively fast track to becoming an owner-CEO, generates attractive financial returns for both investors and searchers, and fosters the development of well-managed, growing businesses. (Stanford GSB,2021).

The term *search fund* was coined at Harvard Business School in 1984 and later gained prominence at Stanford Graduate School of Business during the following decade. Since then, the model has spread steadily to business schools and entrepreneurial communities around the world (Kelly & Heston, 2024). The traditional search fund model was pioneered by Irving Grousbeck as a response to a widespread issue: many small business owners lacked a clear succession plan. While these owners often operated profitable businesses, they typically did not possess the aspiration—or risk appetite—required to lead the company into its next growth phase.

The first search fund, Nova Capital, was raised by Jim Southern in 1984. It marked the model's early success with the acquisition of Uniform Printing, which delivered a 24x return on investment over the subsequent ten years. In its initial phase, the search fund was very much a niche strategy: only 30 funds were raised between 1984 and 1999 (Dennis, 2016). During that period, just 15 to 20 investors accounted for most of the capital deployed in the asset class. This close-knit investor network proved ideal for early searchers, providing both capital and a deep understanding of the strategic levers that drive value creation. As many searchers have later confirmed, mentorship and coaching were critical to the success of these early ETA ventures—and this

pioneering investor group offered both the expertise and the commitment to deliver that support (Dennis, 2016).

Over time, however, the search fund model has expanded significantly, evolving from a niche investment strategy into a globally recognized entrepreneurial acquisition pathway. Notably, more than half of all search funds tracked to date have been launched since 2019, underscoring the acceleration of this model in recent years (Kelly & Heston, 2024). Alongside this growth, both the capital raised for searches and the size of acquisitions have increased dramatically. According to recent studies by Stanford and IESE, total search capital rose from approximately $5 million in 2010 to about $75 million in 2023, while total acquisition volume grew from $110 million to over $880 million during the same period (Kelly & Heston, 2024; Kowalewski et al., 2024). Globally, the trend continues to gain traction, with an additional 320 search funds established in other regions—particularly in Spain and Mexico (Kowalewski et al., 2024). This widespread adoption reflects the transformation of ETA from a specialized asset class into a more institutionalized and scalable entrepreneurial strategy.

1.2.2 Role and responsibilities of the Searcher and the Investor

The search fund model offers a compelling opportunity for both investors and entrepreneurs. For investors, it provides access to a highly inefficient segment of the private equity market—small, profitable companies with $2M to $6M in EBITDA—that are often overlooked by traditional financial buyers (Johnson,2014). These companies typically operate in fragmented markets with limited institutional attention, allowing for attractive acquisition opportunities at reasonable valuations. By backing high-caliber individuals early in their careers, investors can leverage top talent while mitigating the operational risks associated with an inexperienced CEO through their own involvement and support (Johnson,2014).

For the searchers, the model is equally transformative. It creates a path to become a CEO and business owner—often without prior operating experience—while offering meaningful equity upside. This structure enables talented individuals to transition into entrepreneurial leadership roles under the mentorship and guidance of seasoned investors.

The model is based on three fundamental pillars: the **searcher**, the **investor**, and the **target company**.

The Searcher

The searcher plays a central role in managing the fund, conducting the search, and ultimately leading the acquired company. To succeed, they must not only navigate complex deal environments but also develop a strong operational mindset. As Johnson (2014) emphasizes, the most successful searchers are those who are genuinely passionate about building and growing a business. They see the acquisition not as a steppingstone

to another career path, but as a long-term commitment to value creation. Strategic alignment between the company and the searcher's goals—both operational and personal—is essential.

The Searcher's Profile and Competencies

Empirical studies provide a clearer picture of the typical demographic and professional profile of searchers. The median age at the launch of a fund is around 32–34 years, with the majority under 35 (Stanford GSB, 2024). While the model has historically been male-dominated, gender diversity is gradually increasing, with female participation rising from about 10% in 2021 to nearly 18% in 2023 (Stanford GSB, 2024). From an educational standpoint, most searchers hold an MBA—estimates range between 70% and 85%—often completed immediately before launching the fund (Johnson, 2014; Stanford GSB, 2024). Professional backgrounds are most frequently rooted in management consulting, investment banking, private equity, or corporate management, though high-performing cases have also emerged from more diverse profiles (Morrissette & Hines, 2015).

Beyond formal credentials, the literature consistently emphasizes the importance of certain competencies. Leadership and people-management skills are critical, given the rapid transition to the CEO role after acquisition (Johnson, 2014). Resilience and perseverance are equally valued, since the search phase can last up to two years and is often characterized by setbacks and failed negotiations (Morrissette & Hines, 2015). Strong analytical and financial skills are indispensable for deal sourcing, due diligence, and valuation, while sound entrepreneurial judgment enables searchers to identify companies with durable economics and growth potential (Stanford GSB, 2024). Fundraising and communication abilities also play a central role: a typical search requires engaging a syndicate of 15–20 investors and maintaining their support through regular interaction and transparent reporting (Johnson, 2014).

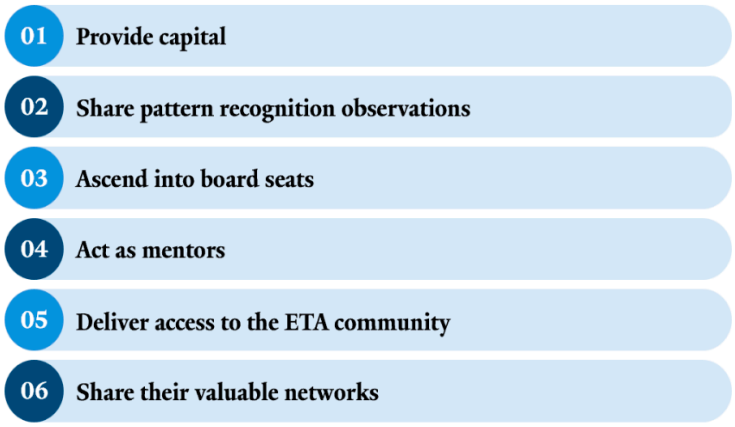
Finally, searchers may pursue the model individually or in pairs. While the solo structure predominates in North America, paired searches are relatively more common in international markets (IESE, 2024). Teams can provide complementary skills and share the workload, yet the evidence on comparative performance remains mixed; ultimately, success depends more on the qualities of the individuals involved and their ability to leverage the mentorship of experienced investors than on the organizational form itself (Stanford GSB, 2024).

The Investor

The composition and engagement of the investor group—often referred to as the cap table—play a crucial role in the fund's outcome. Most investors in search funds are not passive capital providers; rather, they act as mentors, strategic advisors, and sounding boards. Their support is particularly important in the early phases,

where their input can help shape the search strategy, evaluate targets, and negotiate the acquisition. Experienced investors also serve as a safeguard, helping searchers avoid poor acquisitions. Building a cap table of supportive, available, and experienced investors increases the odds of long-term success (Simon,2021).

Figure 1: The six key things search fund investors do for entrepreneurs



Source: Wolfe, 2025

The Target Company

Choosing the right company is arguably the most consequential decision in the search fund journey. High-quality targets typically share a few defining characteristics (Johnson,2014):

- Operation in a growing market
- Strong track record of profitability and revenue growth
- High proportion of recurring or repeat revenue
- Low capital expenditure (Capex) requirements

Searchers are advised to begin by identifying fragmented industries with favorable long-term trends. Within those sectors, businesses that demonstrate stability and downside protection are prioritized. Companies with recurring revenue models and limited Capex demands tend to provide a financial cushion, especially for first-time operators.

Evidence supports this focus: according to the Stanford 2024 Search Fund Study, 80% of early successful acquisitions shared all four of these characteristics (Kelly & Heston, 2024). While some acquisitions that deviated from these criteria also proved successful, they tended to have lower success rates and more variability in outcomes.

This framework has not only proven effective in the United States and Canada, but has also been successfully adapted to international contexts, particularly in Europe and Latin America. The specific dynamics, challenges, and performance of American and international search funds will be discussed in later sections of this thesis, with reference to the 2024 IESE study and 2024 Stanford study.

1.3 The phases of Search Fund Acquisition

The Search Fund model is typically structured around five distinct phases, each of which plays a critical role in the overall entrepreneurial acquisition journey (Morisette, 2015). These phases follow a sequential path, starting from the initial capital raise and culminating in the eventual sale or transition of the acquired business. The following overview provides a high-level summary of each phase, which will be examined in greater detail in the next sections:

- **Fundraising** – This phase involves raising *search capital* from a small group of aligned investors. The capital is used to finance the searcher's salary and essential expenses—such as office space, travel, legal support, and due diligence—for a period typically lasting up to 24 months.
- **Search** – During this stage, the searcher identifies industries and potential target companies, engages with owners, and conducts initial assessments of strategic fit and financial viability. The process is often focused on sourcing proprietary deals and building direct relationships with sellers.
- **Acquisition** – Once a suitable target is identified, the searcher negotiates terms and presents the deal to the original investors, who may exercise their right to participate in the acquisition. The transaction is commonly financed through a mix of equity, vendor financing, bank debt, and contingent mechanisms such as earn-outs.
- **Operation** – After the deal is closed, the searcher steps into the role of CEO and assumes full operational leadership of the company. A Board of Directors—typically composed of several investors—supports the CEO in strategic decisions and governance.
- **Exit** – This final phase includes planning and executing a liquidity event, which may take the form of a strategic sale, private equity recapitalization, or other transition mechanisms. The timing and structure of the exit are influenced by performance, market conditions, and investor expectations.

1.3.1 Fundraising

The fundraising process for most searchers begins well before any formal capital raise and requires careful preparation, self-assessment, and proactive relationship-building. Engaging early with investors, current searchers, and individuals who have successfully exited the model is essential for gaining practical insights and building a reliable support network (Dennis, 2016). A highly effective way to become immersed in the Search Fund ecosystem is through internships with active search funds or institutional investors. These experiences offer exposure to the challenges of the model and simultaneously foster relationships that can prove instrumental during fundraising.

Once this initial network has been developed, the next formal step is the preparation of the Private Placement Memorandum (PPM)—a detailed document that introduces the searcher's background and outlines the fund's structure, investment rationale, and strategic parameters such as industry and geographic focus, budget, and estimated timeline (Stanford GSB, 2021). The PPM is shared with prospective investors ahead of meetings, enabling them to evaluate the opportunity beforehand and assess its fit with their portfolio or strategy.

The PPM also introduces the key financial terms of the investment. These include the structure of capital units, preferred equity rights, and expected return profiles—elements that will later be formalized in the Shareholder Agreement (SHA). The SHA is the legal document that governs the relationship between the entrepreneur and investors after the acquisition, detailing critical aspects such as voting rights, board composition, information rights, and liquidity provisions. While the full agreement is typically finalized at the time of acquisition, initial discussions during fundraising help align expectations and reduce the risk of future conflict (Stanford GSB, 2021).

Typically, capital is raised through units offered to a small group of investors, who are granted preferred equity rights. These include a return of 1.5x their initial investment upon acquisition and the option to participate in the acquisition phase with pro-rata rights. In addition, investors are entitled to receive regular updates on deal flow, key developments, potential targets, and transaction progress throughout the search phase (Stanford GSB, 2021).

Given the multi-year nature of ETA investments, selecting the right investors is a critical success factor—not only in terms of capital contribution, but also in the strategic and operational support they provide. Seasoned search fund investors often bring deep expertise in deal sourcing, evaluation, negotiation, and execution. In many cases, their industry standing and relationships significantly enhance the searcher's credibility with sellers and co-investors, improving the likelihood of closing high-quality transactions (Simon,2021).

Equally important is the internal alignment within the investor group itself: building a cap table composed of individuals who share similar expectations, investment horizons, and communication styles helps prevent friction and facilitates smoother decision-making.

Once committed, the capital raised typically provides an operating runway of up to 24 months. This funding covers essential early-stage costs, including the searcher's salary, travel, office infrastructure, legal and accounting support, and due diligence expenses. Without sufficient resources at this stage, searchers may struggle to maintain momentum, source proprietary deals, or conduct thorough evaluations of target companies (Stanford GSB, 2021).

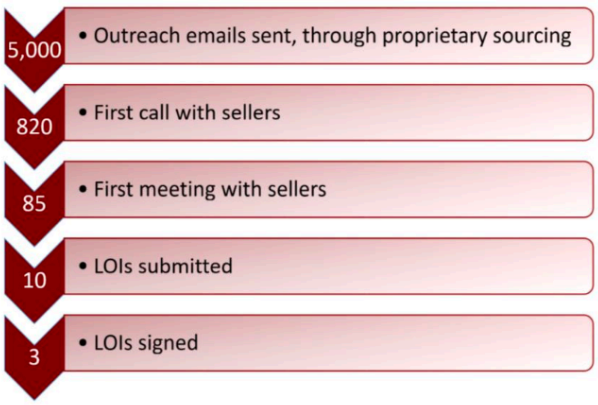
Recent data from the United States and Europe indicate that the median amount raised for a traditional Search Fund ranges between $450,000 and $500,000, with the typical fundraising process taking between three and five months to complete (Kelly & Heston, 2024; Kowalewski et al., 2024).

1.3.2 Sourcing

After completing the fundraising process, the searcher initiates the outreach phase, targeting potential sellers using multiple sourcing strategies to identify high-quality acquisition opportunities. Broadly speaking, these efforts rely on two primary channels: proprietary outreach and broker-mediated deal flow (Stanford GSB, 2021). The relevance of this stage also emerges from the empirical evidence presented later in this thesis, which shows that the superior performance of Search Funds is primarily rooted in disciplined target selection rather than in post-acquisition managerial improvements. This highlights how sourcing is not merely an operational step, but a critical driver of long-term outcomes. Intermediated sourcing—through business brokers or M&A advisors—is a common and accessible approach but often exposes the searcher to highly competitive processes. This typically leads to elevated acquisition multiples and more aggressive timelines, making transactions less favorable for first-time buyers. In contrast, proprietary deal sourcing involves direct engagement with business owners through cold calls and personalized emails (Simon, 2021). While this channel demands significantly more time and persistence, it often results in less competitive bidding environments, more flexible negotiation dynamics, and the possibility of building trust-based relationships over time.

Proprietary sourcing is not only a distinguishing element of the Search Fund model but also one of its most time-consuming components. Studies indicate that it accounts for approximately 25% of the total effort in the pre-acquisition phase (Dennis, 2016). The following funnel provides an illustrative overview of how this outreach process typically unfolds—from initial contact to signed Letters of Intent (LOIs).

Figure 2: Illustrative Search Funnel – Proprietary Sourcing Process



Source: Dennis & Laseca (2016)

The proprietary search process begins with selecting industries that meet key criteria for success—such as fragmentation, growth potential, and low customer concentration. Due to the complexity of industry research and outreach, searchers usually limit themselves to a handful of sectors at a time but may rotate through several over the course of a few months. Once industries of interest are identified, the searcher compiles a detailed list

of potential target companies and their key contacts, particularly business owners and decision-makers. This stage requires extensive data collection and organization (Stanford GSB,2021).

To maximize efficiency, searchers typically conduct in-depth research on three to four industries at a time, refining their focus as they engage with business owners and gather market insights. If a particular sector proves unpromising after initial outreach, they are advised to pivot toward alternative industries. This iterative approach helps balance focus with flexibility during the early stages of the search (Stanford GSB,2021).

To enhance the effectiveness of outreach, searchers often engage "river guides"—industry insiders or consultants who offer expertise and access to networks in exchange for a small percentage of the transaction value (typically 0.5%). These professionals can facilitate warm introductions to business owners, which tend to be significantly more effective than cold outreach alone. In addition to credibility, river guides provide valuable insights into sector dynamics that may not be readily accessible through direct conversations with sellers (Simon, 2021).

Outreach typically occurs through a combination of personalized emails, phone calls, and, in some cases, traditional mail. A best practice is to begin with a customized email, followed by a phone call within a few days. Regardless of the method, the objective is to secure in-person or video meetings as early as possible—not to close a deal immediately, but to build rapport, gather information, and refine the searcher's messaging (Simon, 2021).

These early conversations help the searcher develop industry knowledge, sharpen their acquisition criteria, and gain confidence in deal evaluation. As the process matures, high-quality leads are generated through a combination of direct sourcing, warm introductions, and participation in industry events. Although the process may appear inefficient initially, it is foundational to long-term success, as it strengthens the searcher's ability to assess opportunities, build trust with sellers, and execute informed acquisition decisions (Stern,2014).

Balancing Ideal Conditions with Realistic Opportunities

While a structured acquisition strategy is essential to guide the search process, searchers must also remain flexible. Most businesses will exhibit a combination of strengths and limitations, and very few will align perfectly with initial expectations. The ability to evaluate trade-offs—balancing risk with strategic or financial upside—is often what differentiates successful acquisitions from missed opportunities. In fact, many of the most rewarding search fund investments have involved deviations from original preferences, ultimately justified by strong long-term value potential. Maintaining a pragmatic yet disciplined mindset improves the efficiency of evaluating targets and supports alignment with investors throughout the journey. The specific set of acquisition criteria commonly used in the search fund model will be explored in detail later in this section. (Simon,2021).

Opportunistic Sourcing and Brokered Deal Flow

In addition to proprietary outreach, many searchers complement their efforts through opportunistic sourcing via third-party intermediaries. These include business brokers, boutique M&A advisors, accounting firms, and law practices—professionals who act as intermediaries for business owners seeking an exit. Their role is often pivotal in streamlining initial contact, coordinating documentation, and guiding early negotiations. (Stanford GSB,2021).

To effectively access these opportunities, searchers must invest time in building and managing a dedicated database of contacts. This often involves researching broker networks, attending relevant conferences, and subscribing to deal platforms. Once this infrastructure is in place, searchers typically initiate broad outreach campaigns—often by email—outlining key investment criteria such as revenue size, EBITDA range, target sectors, and ownership transition goals, with the aim of being included in broker mailing lists and staying visible to intermediaries. (Stanford GSB,2021).

Some searchers adopt a more focused approach by developing close relationships with a select group of buy-side brokers. These brokers are incentivized—either through success-based fees or fixed retainers—to actively source deals on behalf of the searcher, often leading to more tailored opportunities and faster deal origination. (Simon, 2021)

Engaging with Investment Banks

Compared to brokers, investment banks present greater access barriers. These institutions typically reserve their deal flow for established private equity funds or repeat buyers with a proven ability to close transactions. For emerging searchers, building credibility with such players requires more than just articulating interest—it demands demonstrating solid investor backing, clarity of purpose, and the ability to act decisively. A strong, reputable cap table can provide the necessary assurance that the searcher has both the means and the advisory support to navigate complex transactions (Simon,2021).

Brokered Deal Advantages and Limitations

One of the primary advantages of brokered deals is that sellers are typically motivated to complete a transaction. This reduces the time and effort searchers must spend educating owners on succession planning or convincing them to consider a sale. In addition, brokers often expose searchers to industries or business models they might not have initially targeted, broadening the scope of viable acquisition opportunities. (Stanford GSB,2021).

However, relying exclusively on brokered channels carries notable trade-offs. Brokers are incentivized to drive up valuations, which can lead to competitive bidding situations where searchers must compete with private equity firms or strategic buyers. Furthermore, in many cases, deals are circulated only after institutional investors have already passed on them—creating a risk of adverse selection. Searchers must therefore approach brokered deal flow with a critical lens, balancing speed and access with thorough due diligence (Simon,2021).

Tapping into Informal Networks

Opportunities are not limited to formal channels. In fact, one of the most overlooked sources of deal flow is the searcher's personal and professional network. By consistently sharing their acquisition objectives—such as company size, location, and transition context—searchers can activate a broad referral network that includes friends, advisors, and community contacts. One notable example involves a searcher who discovered a compelling opportunity through a casual conversation with a family member who had seen a small business for sale in a local newspaper. Such instances highlight the value of remaining visible and communicative even beyond traditional business circles (Simon,2021).

Comparing Proprietary and Brokered Sourcing

Brokered deals offer speed and structure. The seller is typically motivated, and documentation—such as Confidential Information Memorandums (CIMs)—is often complete. These factors allow for faster evaluations and more predictable negotiations. However, this efficiency comes with trade-offs: deals are highly competitive, valuations tend to be inflated, and timelines are tight. Moreover, brokers aim to maximize sale prices and may present deals to searchers only after larger institutional investors have passed, raising concerns about adverse selection. (Stanford GSB,2021).

By contrast, proprietary sourcing gives searchers greater control. Establishing direct relationships with business owners may lead to more exclusive discussions, more favorable terms, and pricing that reflects the true nature of the business rather than auction pressure. But this method requires considerable effort: researching industries, identifying targets, initiating contact, and building trust is a time-consuming endeavor—especially in unfamiliar sectors. Without relevant expertise, searchers risk engaging with businesses they may not be equipped to manage post-acquisition. (Stanford GSB,2021).

The most effective strategies usually combine both approaches. Brokered channels provide scale, while proprietary outreach enhances selectivity and depth. A balanced allocation of time and resources allows searchers to diversify deal flow without compromising focus. (Simon, 2021)

Investor Engagement During the Search

A key component of the scouting phase is the active engagement of the investor base, whose industry expertise,

strategic insight, and extensive networks can greatly enhance the effectiveness of the search. Investors contribute valuable perspectives on macro trends, competitive dynamics, and the relative attractiveness of various acquisition targets. Their input often helps searchers refine their industry focus and identify promising sectors. In some cases, investor connections can lead directly to introductions with business owners, giving searchers access to otherwise unreachable opportunities. (Stern,2014).

To fully benefit from this support, searchers must cultivate strong and continuous relationships with their investor group. Ongoing engagement—both formal and informal—is essential to keep investors aligned and involved. This typically includes regular updates on budget tracking, the deal pipeline, developments with companies at the LOI stage, and upcoming strategic goals. Transparent communication not only strengthens trust but also encourages active participation and guidance.

Within the broader investor base, some individuals naturally assume a more hands-on advisory role. These key investors often engage in regular communication with the searcher, offering mentorship, assisting in deal evaluations, advising on bidding strategies, and helping navigate complex or ambiguous decisions. Importantly, while their financial commitment is the same as that of other investors, their level of involvement and operational insight makes them especially valuable throughout the acquisition process (Stanford GBS,2021).

From Deal Funnel to Shortlist

As the search progresses, searchers typically narrow down a shortlist of 15 to 20 companies warranting deeper analysis. These targets are selected from a broader funnel—built through a combination of brokered introductions, inbound referrals, and proprietary outreach. Initial screening involves reviewing teasers and CIMs, conducting preliminary calls, and evaluating alignment with the investment thesis.

At this stage, searchers often face common obstacles: lack of response, vague financials, or deal terms that don’t meet core criteria. Navigating these challenges requires methodical screening, clear documentation, and frequent re-prioritization. Many searchers implement CRM tools to track interactions and manage the pipeline (Dennis, 2016).

Best Practices in the Sourcing Phase

Regardless of sourcing strategy, three capabilities consistently define successful search efforts:

- Creativity in identifying and approaching business owners

- Discipline in managing outreach volume and frequency
- Organizational rigor in tracking and analyzing deal quality

Equally important is robust data management. Logging contact histories, feedback, and financial insights helps track patterns, optimize future outreach, and streamline decision-making. It also strengthens transparency with investors—an important consideration for both accountability and future capital raising.

Given that sourcing typically spans 18 to 24 months, maintaining discipline over such an extended period is a real challenge. Indeed, historical data shows that about one-third of searchers do not complete an acquisition—highlighting the importance of perseverance, adaptability, and structured execution throughout this phase (Stern,2014).

1.3.3 Acquisition Criteria

Setting clear acquisition criteria is essential for searchers as it establishes a structured approach to evaluating potential targets while aligning expectations with investors. Over time, the search fund community has refined a set of common characteristics that help balance risks and rewards. These criteria guide searchers in identifying businesses with a higher probability of success and mitigating key risks associated with sourcing, acquiring, and managing a company.

The fundamental objective is to acquire a strong business within a promising industry, recognizing that no target will meet all ideal conditions. Searchers must weigh potential trade-offs between business risks and expected returns, carefully assessing opportunities that may deviate from the standard benchmarks but still present an attractive investment (Simon, 2021).

Industry Selection: Identifying Favorable Sectors

At a macro level, defining a clear industry focus increases the efficiency of the search process and improves the likelihood of finding viable targets. Searchers typically begin by analyzing broader industry dynamics to identify sectors with attractive expected growth and sound economics. Industries considered favorable tend to share several attributes (Stanford GBS,2021):

- **Fragmentation** – A market with many small to mid-sized players offers more acquisition opportunities
- **Growth Potential** – Expanding industries present stronger long-term value creation prospects.
- **Size & Scalability** – Larger industries provide a deeper pool of viable targets.
- **Operational Simplicity** – Straightforward business models reduce post-acquisition execution risk.
- **Sustainable Profitability** – Healthy margins (e.g., EBITDA margin >20%) are indicators of financial resilience.

Conversely, searchers tend to avoid sectors with riskier dynamics, such as:

- **Market Consolidation** – Highly concentrated industries leave fewer accessible targets
- **Declining Demand** – Contracting sectors hinder sustainable growth
- **Intense Competition** – Fierce pricing pressure and low entry barriers reduce margin potential.
- **Exogenous Risk** – Industries heavily influenced by regulation or disruption may introduce volatility.
- **Potential for Disruption** – Sectors exposed to rapid technological shifts or new business models (e.g., AI, digitization) may undermine long-term viability and make forecasting difficult.

Company-Specific Criteria: Evaluating Target Businesses

At a micro level, once an industry has been selected, searchers apply additional filters to evaluate individual businesses. The most desirable targets often exhibit the following characteristics:

- **Competitive Advantage** – Strong differentiation or defensible market position.
- **Recurring Revenue** – Predictable cash flows that reduce financial uncertainty.
- **Cash Flow History** – A consistent track record of profitability
- **Motivated Seller** – Ownership transitions driven by personal, not financial, distress.
- **Growth Potential** – Clear opportunities for organic or inorganic expansion.
- **Strong Management Team** – Operational leadership that can support or transition the new CEO.
- **Reasonable Valuation** – A fair price relative to financial fundamentals and risk.

On the other hand, searchers are typically cautious toward companies with the following red flags:

- **Turnaround Situations** – Require significant operational restructuring and execution risk.
- **Customer Concentration** – Dependency on a small number of clients increases revenue volatility.
- **Limited Scale** – Businesses with less than $10 million in revenue or $1.5 million in EBITDA may lack operating leverage.
- **Weak Leadership** – A shallow management bench complicates succession.
- **Competitive Auctions** – High bidder competition tends to inflate valuations.
- **Public-to-Private Conversions** – Often involve added legal and structural complexity.

Together, these industry and company-level criteria serve as a practical filter to narrow the focus on targets that are not only financially sound but also operationally viable for a first-time CEO. (Stanford GBS,2021)

1.3.4 Acquisition

After completing the sourcing phase, the searcher must carry out a comprehensive evaluation of shortlisted businesses to determine the most suitable acquisition target. The acquisition phase itself—excluding the search

process—typically spans between four and twelve months. Its duration depends on several variables, including seller responsiveness, investor engagement, the number of viable targets, the nature of the sourcing channel, and the searcher's ability to manage the transaction process efficiently. Brokered deals tend to progress more quickly due to the early availability of structured financial and operational data, whereas proprietary deals often require more time to collect and validate key information (Simon, 2021). Although not explicitly disaggregated in most datasets, this estimate aligns with the average end-to-end timeline reported by Stanford, where the combined search and acquisition process lasts approximately 22 months (Kelly & Heston, 2024).

Effective time management is essential throughout the acquisition process, particularly given the financial and temporal constraints under which most searchers operate. Each transaction represents a strategic allocation of limited resources. For this reason, it is crucial to define clear priorities and concentrate on decision-driving variables, avoiding the pitfalls of excessive or unfocused analysis. A methodical approach not only improves the efficiency of due diligence but also facilitates risk assessment, feasibility analysis, and negotiation planning (Stanford GBS,2021).

Maintaining a transparent and constructive relationship with the seller is equally vital. Trust-building enhances the likelihood of a smooth transition and increases the probability of deal completion. Searchers should also periodically reassess the opportunity, as both internal dynamics and external conditions may evolve during the negotiation and evaluation process. Without disciplined time and resource management, there is a heightened risk of deal fatigue, missed windows of opportunity, and suboptimal execution. For many searchers, this phase represents their first experience leading a transaction of this complexity—making a structured and intentional approach even more critical (Simon,2021).

While the acquisition process may vary considerably across search funds, it typically unfolds in three main stages, each designed to assess the viability and structure of the potential transaction:

1. Preliminary due diligence
2. Valuation and execution of a Letter of Intent (LOI)
3. Comprehensive due diligence

Preliminary Due Diligence

Once a business owner expresses interest in a potential sale, the searcher initiates a preliminary assessment to determine whether the opportunity warrants further analysis and resource allocation. At this stage, the valuation of the target company is based on limited data and broad assumptions, often derived from basic indicators such as revenue figures, operating margins, customer retention metrics and Annual Recurring Revenue (ARR). The objective is twofold: to assess whether the business aligns with the search fund's strategic and financial criteria, and to evaluate the seller's motivation and seriousness regarding the transaction (Stanford GBS,2021).

When an advisor is involved, the seller will typically provide a Confidential Information Memorandum (CIM). In proprietary situations, however, documentation tends to be less formalized, and the searcher may need to rely on summary financial statements or direct conversations with the owner. At this point, feedback from investors is also essential, as they possess the right—but not the obligation—to participate in financing the acquisition. Early alignment with the cap table ensures efficient use of time and avoids advancing opportunities that may not secure the necessary backing.

This high-level screening process generally produces:

- A ranking of the opportunity relative to other active targets
- A preliminary valuation range based on comparable transactions or heuristics
- A summary of key advantages, risks, and sector-specific considerations

In some cases, this stage culminates with the signing of an Indication of Intent (IoI)—a non-binding document in which the searcher proposes an estimated valuation range and outlines any specific requests for further information. Although not legally enforceable, the IoI serves a critical function: it creates a mutual understanding of valuation expectations before entering a more resource-intensive stage of analysis, allowing both parties to proceed with greater clarity and alignment (Stanford GBS,2021).

Valuation and Letter of Intent (LOI)

The second stage of the acquisition process plays a pivotal role in validating the feasibility of the transaction and aligning all parties involved. At this point, the searcher must evaluate several core elements:

- The seller's willingness to proceed and close the deal
- The interest and commitment of investors to finance the acquisition
- The strategic and financial fit of the company, including its alignment with industry dynamics, valuation expectations, and the desired business model

This step acts as a formal checkpoint before advancing to comprehensive due diligence. To make an informed decision, the searcher typically requests detailed financial and operational information, including historical and projected income statements, key performance metrics, and customer-related data such as concentration levels and churn. These inputs are essential for assessing sustainability and for preparing internal valuation models (Stanford GBS,2021).

During this phase, the interaction between the searcher and the seller intensifies. For many business owners—particularly those targeted by search funds—this represents their first experience navigating a formal sale process. As such, they may find the process stressful or invasive, especially when confronted with requests for granular financial, strategic, or operational data. Many small and medium-sized businesses operate with informal reporting systems and rely heavily on the founder's tacit knowledge, rather than structured analytics.

Consequently, the information needed by the searcher is not always readily available and must often be developed collaboratively (Stanford GBS,2021).

Managing this dynamic is critical. Excessive or poorly framed requests may overwhelm the seller, erode trust, and jeopardize the transaction. Clear, respectful communication is therefore essential. The searcher should explain why certain information is needed, how it will be used, and the importance of timing. Prioritizing critical issues and avoiding exhaustive data requests can help maintain momentum and goodwill. When direct documentation is unavailable, alternative methods—such as using existing reports, management interviews, or targeted discussions with key stakeholders—can offer valuable insights with less disruption (Simon, 2021). By demonstrating transparency, adaptability, and empathy throughout this stage, the searcher not only improves the quality of due diligence but also strengthens the foundation for a successful deal and post-acquisition transition (Stanford GBS,2021).

The ultimate objective of this stage is to reach an agreement on a Letter of Intent (LOI), which formalizes key terms of the deal before entering comprehensive due diligence. To reach that point, the searcher must first conduct a more structured financial and strategic assessment of the target. The most used method for preliminary valuation in the Search Fund context is the precedent transaction approach, which applies market multiples derived from comparable private acquisitions. In parallel, the searcher may use a simplified buyout model to estimate projected returns—including Internal Rate of Return (IRR) and Return on Investment (ROI)—based on assumptions about purchase price, capital structure, and exit multiple scenarios.

In this framework, Adjusted EBITDA serves as the central valuation metric. As highlighted in the Stanford Search Fund Primer (Stanford GSB, 2021), Adjusted EBITDA represents a normalized measure of earnings that excludes non-recurring, discretionary, or non-operational items. It not only underpins deal pricing but also informs debt sizing, covenant setting, and performance benchmarks. A clear understanding of how adjustments are calculated is therefore essential to avoid mispricing and ensure financial alignment across all stakeholders.

Other methods may be used to triangulate results:

- **Public comparable**, which apply trading multiples from publicly listed companies in similar industries, adjusted downward to reflect size and liquidity discounts
- **Discounted Cash Flow (DCF)** analysis, which estimates the present value of projected future cash flows based on a cost of capital benchmarked against industry peers. While theoretically robust, DCFs are rarely decisive in ETA transactions due to the limited availability of long-term forecasts and the high uncertainty involved.
- **Asset-based valuation**, which estimates value based on the net book or liquidation value of tangible assets. This method is generally less relevant for search fund targets, which tend to be profitable, cash-flow-generative businesses—often in services—where intangible assets and growth prospects carry more weight (Stanford GSB, 2021).

Once valuation assumptions have been validated and investor alignment is secured, the searcher may proceed to propose a Letter of Intent. The LOI is a non-binding agreement that lays the foundation for final negotiations and confirms mutual commitment to advance toward closing.
Key elements of the LOI typically include:

1. An agreed-upon purchase price or valuation range
2. Indicative deal structure (equity, seller financing, earn-out)
3. Preliminary terms regarding employment agreements, transition period, and governance
4. A binding "no-shop" clause, which grants the searcher exclusivity for a defined period
5. An indicative timeline with milestones for due diligence, contract signing, and closing
6. A preliminary outline of the due diligence scope, clarifying the main areas to be reviewed (financial, legal, tax, and operational)

While non-binding in most respects, the LOI is critical to aligning expectations, enabling access to sensitive information, and protecting the searcher from competing bids while due diligence is underway. It signals to both the seller and the investor group that the deal has reached a serious and actionable phase.

Due Diligence

The final stage before completing the acquisition is the comprehensive due diligence process. This phase typically spans between 30 and 120 days and represents a critical opportunity for the searcher to validate all key assumptions underlying the deal (Stanford GSB, 2021). The objective is twofold: to identify material risks—financial, operational, legal, or strategic—and to refine the structure and terms of the transaction accordingly. In parallel, this process serves to prepare the searcher for post-acquisition ownership by deepening their understanding of the business's inner workings.

The duration and complexity of this phase can vary significantly depending on the nature of the business. For example, asset-light service companies typically require a more straightforward analysis, whereas asset-heavy businesses may involve extensive verification of physical assets, inventories, or supply chains. Likewise, companies with international operations or foreign subsidiaries often demand additional legal, tax, and regulatory due diligence. These factors influence not only the scope of the analysis but also the type and number of external advisors involved (Stanford GSB, 2021).

A crucial dimension of due diligence is the evaluation and refinement of the deal's capital structure. The choice of financing mix is not merely technical—it directly influences the overall risk-return profile of the transaction. Since Search Fund acquisitions resemble small-scale leveraged buyouts, financial leverage can be a powerful driver of value creation. However, it must be employed judiciously. Most target companies are small, founder-

led businesses with limited formalization and potentially fragile financial structures. Overleveraging may reduce operational flexibility or heighten vulnerability in periods of stress.

A sustainable and well-calibrated capital structure—tailored to the company's cash flow and strategic context—is therefore essential. Most deals rely on a combination of the following instruments (Stanford GSB, 2021):

- **Preferred Equity**: Typically includes liquidation preferences and guaranteed returns to early-stage investors, especially those who funded the search phase.
- **Mezzanine Debt**: Subordinated debt that bridges the gap between senior loans and equity, often carrying higher interest or equity-like features.
- **Earnouts**: Contingent payments tied to future performance metrics, useful to align incentives and manage valuation uncertainty.
- **Seller's Loan**: Deferred consideration provided by the seller, often with subordinated repayment and negotiated interest.
- **Senior Loan**: The primary form of secured lending, backed by the target company's assets and cash flows, and typically provided by banks or credit funds.

Finding the right balance among these sources helps to ensure financial sustainability while aligning interests across stakeholders. While more aggressive capital structures may improve projected returns, conservative approaches tend to offer greater resilience, particularly in deals involving first-time operators or businesses with limited reporting infrastructure.

Unlike institutional buyers, search fund entrepreneurs typically lack large in-house due diligence teams. As a result, they must adopt a focused and efficient approach, dedicating their own efforts to core analyses and selectively engaging third-party professionals where needed. Legal and accounting advisors are almost always involved, particularly for reviewing contracts, verifying compliance, and validating financial statements. Depending on the business and sector, additional specialists—such as environmental auditors, IT consultants, or industry experts—may be brought in for targeted assessments.

Due diligence findings can significantly affect the deal structure. If key issues are uncovered—such as customer concentration, margin volatility, or pending litigation—the searcher may renegotiate the purchase price or adjust the deal through mechanisms such as (Stanford GSB, 2021):

- **Seller financing**, which aligns incentives and defers part of the payment
- **Earn-outs,** which tie a portion of the price to future performance milestones
- **Indemnities**, which protect the buyer from future liabilities

These tools help mitigate downside risk without necessarily derailing the transaction. The involvement of experienced investors at this stage is especially valuable, as they can provide technical guidance, negotiation support, and decision-making discipline.

Beyond risk mitigation, due diligence also has a strategic dimension. By engaging with the company's leadership, employees, customers, and suppliers, the searcher gains first-hand insights into culture, processes, and growth opportunities. This knowledge is essential for shaping the initial 100-day plan and preparing for the CEO transition (Simon,2021).

Ultimately, comprehensive due diligence is not only a protective step, but also a formative one: it transforms the searcher from external acquirer to informed operator. A well-executed diligence phase increases the probability of a smooth transition, positions the business for early wins, and lays the foundation for long-term value creation (Simon,2021).

Sale and Purchase Agreement

In Search Fund acquisitions, the Sale and Purchase Agreement (SPA) serves as the definitive legal document that formalizes the transition of ownership. While its structure resembles that of traditional M&A contracts, there are specific nuances that reflect the nature of ETA transactions. One such aspect is the relationship dynamic: Searchers are often first-time buyers acquiring businesses from founder-owners, which makes it especially important to balance legal protections with a respectful and collaborative tone (Simon,2021).

It is common for SPAs in Search Funds to include earnout provisions, allowing part of the purchase price to depend on the company's future performance. These mechanisms help reconcile valuation expectations and are particularly useful when sellers remain emotionally invested in the business. Additionally, working capital adjustments are frequently used to align the final purchase price with the company's actual operating condition at the time of closing, especially given the often informal or outdated financial reporting systems of small and mid-sized enterprises (Stanford GSB, 2021).

Post-closing obligations are another area of focus. These may include non-compete agreements, support during the transition period, or restrictions on seller actions prior to closing. Because many sellers have limited experience with complex legal documents, it is critical for the searcher to clearly explain the purpose and implications of SPA provisions early in the negotiation process. This proactive communication helps prevent misunderstandings, maintains trust, and increases the likelihood of a successful closing (Simon,2021).

1.3.5 Operation

Following the acquisition, the focus of the Search Fund shifts from sourcing and deal execution to the complex task of operating and growing the acquired company. This stage represents both the greatest challenge and the ultimate test for the entrepreneur, who must transition into the role of CEO and assume full responsibility for

the firm's strategic direction, organizational structure, and long-term performance. While the empirical evidence presented in Chapter 3 and 4 suggests that Search Funds do not systematically deliver superior post-acquisition improvements compared to Private Equity, the operational phase remains critical for ensuring stability, sustaining the advantages of a well-selected target, and building the foundations for long-term value creation. The following sections highlight the key dimensions of this transition—leadership handover, strategic communication, early management practices, governance, and value creation—drawing on the literature and practical experience to illustrate how newly appointed CEOs can navigate the complexities of leading a small or medium-sized enterprise acquired through a Search Fund

Leadership Transition and Knowledge Transfer

After completing the acquisition, it is essential to establish a clear and structured transition plan. While there is no universal approach, it is common for the searcher to assume the role of CEO shortly after the deal closes. In some cases, the previous owner exits the company entirely, whereas in others, they remain involved for a defined transition period to support knowledge transfer and ensure continuity. To manage this phase effectively, it is advisable to formalize the arrangement through a Transition Services Agreement (TSA)—a legal contract that outlines the scope, duration, responsibilities, and expectations of the seller's involvement during the handover. A well-defined TSA helps minimize ambiguity, aligns both parties on key milestones, and supports a smoother leadership transition (Simon, 2021).

Strategic Communication in the First Months

The literature underscores the critical role of strategic communication in the early stages following an acquisition. Simon (2021) emphasizes the importance for searchers to develop a detailed stakeholder map, identifying all key internal and external parties, and to design a targeted communication plan that proactively addresses the specific concerns and expectations of each group. While standard communication efforts typically include employees, customers, and suppliers, each small to mid-sized enterprise (PMI) has its own unique stakeholder landscape that must be carefully considered.

An effective communication strategy involves crafting tailored messages for each stakeholder group and preparing thoughtful responses to anticipated questions. Concerns may range from job security and working conditions for employees, to pricing, contract terms, and service continuity for customers and suppliers. According to the *Search Fund Primer* (Stanford GSB, 2021), this phase presents a valuable opportunity to establish trust and credibility through clear, transparent, and consistent messaging. Early, well-structured

communication helps foster a collaborative environment, reinforces confidence in the new leadership, and lays the foundation for a smooth and successful transition.

The First 100 Days: Observation and Systems Building

Another key concept highlighted in the literature is the importance of the first 100 days roadmap following an acquisition. This initial phase is critical for the new CEO to gain a deep, hands-on understanding of the business. Rather than implementing immediate changes, the focus should be on learning and observation across all business functions, with particular attention to operational dynamics and organizational culture. During this time, the new leader is expected to listen actively to employees and former managers, while carefully observing day-to-day operations to understand internal processes and pain points.

A second major priority of this phase is the design and implementation of a robust managerial reporting system. Establishing clear and reliable reporting mechanisms enables better strategic planning, performance tracking, and long-term value creation. These systems provide the searcher-CEO with the tools to monitor performance, allocate resources effectively, and make informed decisions. Core components typically include a clear understanding of cash expenditures, cash flow behavior, working capital management, and the definition of key operational KPIs.

Among these, establishing relevant Key Performance Indicators (KPIs) is particularly critical, as they serve as practical drivers to align daily operations with strategic goals. KPIs should be clear, straightforward, and logically connected to the business's core activities, enabling teams at all levels to focus on what truly matters for sustainable growth and operational excellence (Simon,2021).

Search Fund company's Board

As noted by Wasserstein (2018), the relationship between a search fund CEO and the board differs significantly from that in a typical private equity setting. While PE-backed CEOs are often experienced operators appointed by a controlling firm, search fund CEOs are usually first-time leaders supported by a broad base of passive investors. In the absence of a dominant shareholder, the board typically takes on a more hands-on role—providing mentorship, filling gaps in experience, and supporting key strategic decisions.

Given this central role, assembling the board becomes one of the CEO's first and most consequential tasks after the acquisition. Search fund boards generally consist of three to eight members (Wasserstein, 2018). In building the board, the CEO should prioritize individuals who are accessible, engaged, and bring relevant operational or financial expertise. Those with prior experience in small business acquisitions or scaling companies can be particularly valuable during the transition. While some investors may request board seats, appointments should be based on the ability to contribute meaningfully—not just on capital invested. Well-

composed board can become one of the CEO's greatest assets—offering strategic guidance, expanding credibility with stakeholders, and helping to ensure long-term success. In conclusion, the board's role in a search fund is to actively support the CEO as both advisor and partner. Rather than simply overseeing decisions, board members are expected to challenge ideas constructively, offer guidance, and help the CEO grow into the role. Inexperience is common, so the board must focus on building trust, encouraging transparency, and contributing to thoughtful, long-term decision-making. A strong board can meaningfully increase the chances of success by helping the CEO lead with clarity and confidence.

Long-Term Value Creation

After the transition phase, the searcher must shift focus toward long-term value creation. This involves defining and communicating a clear strategic vision, grounded in the company's operational reality and supported by its management team. One of the core advantages of the Search Fund model is the ability to build a robust, scalable platform for future growth, leveraging four key value drivers (Simon,2021):

- **Revenue Growth**: Expanding sales through pricing optimization, customer acquisition, and new market opportunities.
- **Operational Efficiency**: Enhancing productivity and reducing costs to improve margins and resource utilization.
- **Deleveraging**: Managing debt to improve financial resilience and reduce risk exposure.
- **Multiple Expansion**: Increasing the company's valuation by strengthening its market positioning, governance, and long-term performance outlook.

Central to these efforts is the refinement of the company's business model—shifting, for example, from transactional to recurring revenues, increasing pricing power, or raising customer retention. Improvements that enhance the predictability and quality of earnings are particularly valuable, as they tend to support stronger EBITDA multiples.

The most responsibility of the CEO in this phase is the strategic allocation of capital. Effective leaders must decide where and how to deploy cash—whether reinvesting in high-ROI initiatives, refinancing to reduce the cost of capital, or returning funds to shareholders when internal opportunities are limited. Capital allocation decisions should be consistent with the company's long-term priorities and cash flow profile and regularly reviewed to adapt to changing circumstances. As highlighted in the literature, mastering this function can be a key differentiator in the creation of shareholder value (Simon,2021).

1.3.6 Exit phase

The timing of the exit depends on several factors, including the structure of the cap table—particularly the presence of institutional investors with liquidity constraints—as well as prevailing market conditions.

According to Dennis and Laseca (2016), the average holding period for a Search Fund is approximately seven years, longer than for most financial buyers. This reflects the long-term value creation approach inherent to the model.

Simon (2021) emphasizes the importance of careful legal preparation during the exit phase. In particular, he highlights the need to involve legal advisors early in the process to clarify transaction terms, address regulatory complexities, and protect the interests of both the entrepreneur and the investor group.

Searchers must also become familiar with the different exit pathways available and understand how businesses in their sector are typically valued. The five most common exit strategies include:

- **Recapitalization**
- **Replacement capital**
- **Trade sale to a financial buyer**
- **Trade sale to an industrial buyer**
- **Initial Public Offering (IPO)**

Recapitalization

When a company continues to grow but a full exit is not yet optimal, recapitalization can be an effective strategy. This approach involves restructuring the capital stack by leveraging new debt to provide liquidity to existing shareholders—often via dividends or share repurchases. It enables investors and entrepreneurs to partially monetize their equity while retaining ownership and operational control. Recapitalizations can occur multiple times throughout the life of the business and are particularly attractive to entrepreneurs who wish to remain actively involved in driving future growth. Investors benefit by receiving earlier cash distributions, which can improve their IRR even in the absence of a full exit.

Replacement Capital

Replacement capital involves the entry of new shareholders—typically private equity funds—who acquire equity directly from existing investors. Unlike a growth equity investment, this transaction does not add new capital to the company's balance sheet but provides direct liquidity to outgoing stakeholders. These buyers generally favor continuity in leadership and do not require major changes in strategy or governance. Their investment horizon is often longer, making this a useful option when the founder seeks liquidity while continuing to lead the business through its next phase.

Trade Sale to an Industrial Buyer

A trade sale to an industrial (or corporate) buyer consists of selling the company to another operating business, usually within the same sector. This path frequently delivers the highest valuation, as strategic acquirers can benefit from synergies in operations, market access, and technology. However, such deals often require a defined transition period during which the entrepreneur assists in integration efforts. Cultural shifts, new reporting lines, and loss of autonomy may make this option less attractive to some searchers, particularly those who value independent leadership roles.

Trade Sale to a Financial Buyer

A trade sale to a financial buyer, such as a private equity fund, centers on financial performance and future upside potential. These buyers typically rely on robust cash flow, strong KPIs, and the possibility of leveraged returns. Entrepreneurs often remain onboard for a set period, and in many cases, are required to reinvest a portion of their proceeds—commonly around one-third—into the business to ensure alignment. While continuity is often valued, some financial buyers may seek leadership changes or strategic realignment. Understanding the specific track record and approach of the buyer is essential before closing the transaction.

IPO

An IPO allows a company to access public capital markets and provides an eventual exit path for both the entrepreneur and investors. However, liquidity is not immediate: existing shareholders are generally subject to lock-up periods (typically six months), during which they cannot sell shares. IPOs also change the nature of the CEO role, requiring more focus on investor relations, compliance, and public disclosures. While some entrepreneurs embrace this transition, others may prefer roles centered on operational execution rather than external communication and regulatory engagement.

Ultimately, the optimal exit route depends on a variety of factors: the company's stage of maturity, the preferences of the investor group, prevailing market conditions, and the entrepreneur's long-term goals. For this reason, the exit phase must be treated with the same strategic rigor as the acquisition itself—balancing liquidity with continuity, and short-term gains with sustainable value creation.

As the exit strategy begins to take shape, a structured and forward-looking approach becomes essential. According to Simon (2021), no exit decision should be undertaken without first reviewing the governance framework outlined in the shareholder agreements. These documents often include critical provisions—such as board approval thresholds, tag-along and drag-along clauses, and IPO-related rights—that can significantly influence both the feasibility and structure of the transaction. Understanding these elements early can help prevent misalignment and procedural delays during deal execution.

Equally important is the assessment of timing. Exit readiness does not depend solely on internal performance; it also hinges on broader market conditions and investor expectations. A high-functioning board of directors plays a key role in evaluating these factors, helping the entrepreneur determine whether to pursue an exit, delay for strategic reasons, or consider alternative outcomes such as a partial recapitalization. In some cases, revisiting the incentive structure for the CEO and management team may also be warranted—especially if holding periods extend beyond the original investment horizon (Simon,2021).

Real-world cases like *OnRamp Prepares for an Exit (A)* and *(B)* illustrate how successful exits are rarely opportunistic. Rather, they reflect deliberate preparation and ongoing dialogue between the entrepreneur, board, legal counsel, and potential buyers. In these examples, early engagement with investment bankers, pre-alignment on governance rights, and scenario modelling proved instrumental in shaping a credible and executable exit strategy.

As such, search fund entrepreneurs are advised to treat exit preparation not as a final step, but as an integral part of long-term planning—one that begins well before the first bid is received. This mindset ensures that when a favourable opportunity does arise, the company is not only financially ready, but also organizationally aligned and legally prepared to deliver a successful outcome for all stakeholders.

Chapter 2 - Strategic, Economic and Geographical Dimensions of The Search Fund Model

2.1 Search Funds economics

2.1.1. The compensation structure

The search fund model employs an economic structure designed to align risk, incentives, and capital preservation for both investors and the entrepreneur. Typically, the acquisition is financed through a participating preferred equity structure, which grants investors the right to recover their initial capital and a predefined return before the entrepreneur participates in equity distributions. This mechanism offers downside protection for investors while preserving incentive alignment with the searcher (Stanford GSB, 2021).

Investor protections generally take two forms. First, investor capital enjoys seniority over the searcher's equity—commonly referred to as a liquidation preference—ensuring that investors are repaid first in the event of a sale or liquidation. Second, many search fund deals include a preferred return, typically structured as an annual dividend on preferred shares or as interest on a note, which enhances investor yield before any distributions are made to the entrepreneur (Goel,2023).

Searcher equity is usually issued in the form of common shares and only accrues value once investors have recovered their capital and associated preferred return. Investor contributions are made in two stages: search

capital, generally between $400,000 and $500,000, finances the sourcing phase; acquisition capital, significantly larger, is deployed at the time of purchase and depends on the target company's size and the capital structure. Upon closing, search capital is commonly converted into equity—often with a step-up of approximately 150%—to compensate early backers for their elevated risk exposure. A key instrument in the capital stack is participating preferred equity. Subordinate to debt but senior to common equity, it entitles investors to receive their initial investment and any unpaid preferred return, followed by a share of remaining equity at exit. Depending on the agreement, preferred equity may be redeemable or remain in place until a defined liquidity event.

The searcher's equity package is typically structured in three distinct tranches; each tied to a specific milestone or performance objective (Stanford GSB, 2021). The first tranche, representing one-third of the total potential equity, is granted upon the successful acquisition of the target company. The second tranche vests progressively over time—commonly following a four- to five-year ratable schedule during the searcher's tenure as CEO. The final tranche is performance-based and contingent on delivering superior returns to investors. Performance equity is usually tied to the internal rate of return (IRR) achieved upon exit, with vesting thresholds ranging from a minimum floor of 20% to a cap of 35%**,** beyond which full performance equity is granted. Vesting within this range occurs on a linear, pro-rata basis. For example, if a searcher achieves a 28% IRR, the difference from the 20% floor is 8 percentage points. This corresponds to approximately 53% of the performance tranche being earned (8 ÷ 15). If the eligible performance tranche is 8.33% (one-third of a 25% equity package), the searcher would vest approximately 4.4% additional equity (Goel, 2023)**.** Importantly, this IRR threshold refers to the net IRR delivered to investors, meaning it reflects returns after accounting for the entrepreneur's equity allocation. Some search funds may use Multiple of Invested Capital (MOIC) as an alternative performance benchmark, though IRR remains more common due to its sensitivity to timing and capital deployment.

Overall, search fund entrepreneurs typically vest into 25–30% of the common equity, with solo searchers often capped at 25%, and partnerships eligible for up to 30%. This structure aims to create alignment by rewarding long-term commitment, disciplined execution, and exceptional investor outcomes.

Figure 3: An Illustrative ETA Waterfall

Source: Goel, 2023

Challenges with Preferred Equity

While preferred equity is central to investor protection, it may also create unintended consequences for incentive design. When a preferred return is layered on top of IRR-based vesting, the compounding of hurdles can reduce the searcher's upside at moderate exit outcomes. For example, a small increase in investor returns due to preferred dividends can significantly cut the entrepreneur's equity—potentially by more than 20%—while increasing investor IRR by less than 1% (Stanford GSB, 2021). This asymmetry may dilute motivation at critical inflection points.

IRR vs. MOIC: Incentive Design Trade-Offs

A central debate in search fund economics concerns the performance metric governing equity vesting—specifically, IRR versus MOIC (Multiple of Invested Capital). IRR, long favored in private equity, incorporates the time value of money and encourages capital efficiency. However, its use in search funds may incentivize early exits that optimize timing at the expense of long-term value creation. In contrast, MOIC emphasizes total value over time but may lead to holding periods that are unnecessarily prolonged. Both metrics, when applied in isolation, risk distorting behavior. To mitigate this, some funds adopt hybrid structures—applying MOIC targets in the earlier years and IRR hurdles later in the investment cycle. This blended approach aims to balance timing pressure, capital returns, and the maturing capabilities of the searcher as a first-time operator (Johnson,2017).

2.1.2 Return of Search fund

Financial Performance of North American Search Funds

Search funds in the U.S. and Canada have historically delivered strong but uneven returns. As of December 31, 2023, the aggregate internal rate of return (IRR) across all search funds was 35.1%, with an average MOIC of 4.5x. Funds that completed an acquisition and exited reported an IRR of 42.9%, while the most recent cohort (2021–2022) posted an early-stage IRR of 23% and MOIC of 1.5x. The median holding period for exited companies was 5.9 years, with cohort variations ranging from 4.4 to 7.9 years (Kelly & Heston, 2024).

Return dispersion is notable. Among 296 companies with MOIC data, 31% led to total or partial capital loss, while 69% generated positive returns: 27% achieved 1–2x, 36% reached 2–5x, 25% exceeded 5x, and 11% produced returns greater than 10x. Similar variability is evident in IRR results, with 52% of 200 companies posting IRRs between 1%–25%, and 6% exceeding 75%. Interestingly, although partnered searchers

outperformed solo searchers on average (40.5% vs. 30.3% IRR), five of the six most recent 10x or plus ROI deals were executed by solo operators (Kelly & Heston, 2024).

On the operational side, the median acquisition price was $14.4 million, with EBITDA margins averaging 27% and top-line growth rates at 25%. These companies were acquired at an average EBITDA multiple of 7.0x. For searchers, average equity value for exited CEOs was $5.7 million (median: $2.25M), while current operators reported $6.09 million on average (median: $1.98M). However, it is important to note that 37% of the 681 total search funds did not complete an acquisition and therefore generated no returns.

Financial Returns of International Search Funds

Outside North America, search funds report more modest yet solid results by entrepreneurial benchmarks. Based on 130 international search funds with IRR and MOIC data, —93 with acquisitions and 37 without. As of December 31, 2023, the aggregate MOIC was 2.0x and IRR 18.1%. Excluding terminal funds, MOIC for active acquisitions was 2.1x with an IRR of 19.6%, whereas exited funds recorded MOIC of 1.9x and IRR of 17.3% (Kowalewski et al., 2024).

Returns are highly skewed. The median MOIC is 1.4x, with the best-performing fund achieving 31.4x, significantly lifting the average. Removing top outliers drops aggregate performance sharply. Partnered search funds (35% of the total) had slightly better odds of achieving >10x ROI than solo searchers (5% vs. 2%), though overall performance distribution between the two structures was comparable.

Operationally, acquisitions tend to be smaller than in the U.S. and Canada, though median deal size is not specified. Entrepreneurial equity outcomes, however, appear consistent with North American figures, with exited CEOs reporting $5.7M and active operators averaging $6.09M. Still, caution is warranted given the lower availability and reliability of international data. Consistent with U.S. trends, a substantial portion—between 20% and 30%—of international search funds never completed an acquisition, yielding no investor returns (Kowalewski et al., 2024).

2.1.3 Risk inherent to the model

Although search funds have delivered compelling returns in aggregate, the model entails a unique set of risks—many of which are intrinsic to its structure and execution rather than to market cycles. In *Search Funds: Death and the Afterlife*, the authors examine the root causes of failed investments through interviews with searchers and investors involved in underperforming or collapsed acquisitions. The study identifies nine recurring risk factors that often contribute to negative outcomes:

1. **Low or negative industry growth**, limiting the company's capacity for long-term expansion
2. **Operational complexity**, which can overwhelm first-time CEOs with limited experience
3. **Board dysfunction**, leading to strategic misalignment and impaired decision-making

4. **Low gross margins**, reducing operational flexibility and delaying value creation
5. **Execution failures**, stemming from poor leadership or mismatched strategy
6. **High customer concentration**, increasing revenue risk and dependency
7. **Restrictive capital structures**, limiting maneuverability in times of stress
8. **Conflict with the previous owner**, disrupting post-acquisition transition
9. **Talent retention issues**, particularly in key roles critical to continuity and growth

These risk factors suggest that a substantial portion of failure cases are not due to flawed acquisitions per se, but rather to challenges that arise after the transaction closes. A recurring theme is the gap between the entrepreneurial ambition of the searcher and the operational realities of running a small to mid-sized business. Similarly, governance issues—particularly in cases of misalignment between the searcher and the investor-led board—can severely impede strategic execution.

Even with a strong target company, the transition to ownership represents a high-stakes bottleneck in the search fund process. As highlighted in *Death and the Afterlife*, these structural risks underline the need for robust support systems, both at the governance level and within the operating environment.

Interpreting the Risk-Return Trade-off in Search Funds

The coexistence of high aggregate returns and high failure rates in search funds reflects a core characteristic of entrepreneurial investing: outcomes are both uncertain and heavily skewed. According to Kelly & Heston (2024), U.S. and Canadian search funds have generated an aggregate IRR exceeding 35%, but approximately 31% of completed acquisitions have resulted in a full or partial capital loss. International funds show more modest but still positively skewed outcomes, with median ROIs significantly below the mean (Kowalewski et al., 2024). In both contexts, a substantial proportion of launched funds—around one-third—never close a deal, yielding zero returns.

These dynamics highlight a fundamental truth: while the model has demonstrated exceptional upside potential for both investors and entrepreneurs, the path to success is far from guaranteed. Execution risk plays a decisive role. The steep learning curve of operating a business, combined with the pressure to deliver investor returns, can expose gaps in leadership capability or decision-making discipline. This tension underscores a central paradox of the search fund model: while it grants accelerated access to the CEO role, it demands competencies that typically require years of real-world experience.

As such, the model is best suited for individuals who combine strong leadership potential with high resilience and a robust support network of experienced investors. Without these ingredients, the risks—especially post-acquisition—can quickly outweigh the potential rewards.

2.2 Search Fund in Europe

A comparative view of search funds in the U.S. and Canada versus those operating internationally reveals meaningful differences across fundraising dynamics, deal structures, and performance metrics. U.S. and Canadian searchers typically raise capital faster, with a median fundraising period of 3 months, compared to 5 months internationally. The median amount of search capital is also higher in North America—$500k versus $456k—whereas partnerships are more common internationally (35% vs. 19% in the U.S.) and solo searchers tend to raise less on average.

Target industries also differ. While both regions show strong interest in tech-enabled services, healthcare, and traditional services, international searchers place greater emphasis on manufacturing and logistics. Meanwhile, software—previously dominant in the U.S.—has seen a relative decline. These preferences affect acquisition multiples: U.S. deals report higher median purchase price to EBITDA multiples (7.0x vs. 5.7x), as well as slightly higher purchase price to revenue ratios (1.8x vs. 1.4x). Median acquisition size is also larger in the U.S. ($14.4M vs. $11.7M), with companies showing higher EBITDA margins (27% vs. 24%).

Holding periods for exited companies are slightly longer in North America, with a median of 5.9 years (ranging up to 7.9), compared to 5.3 years internationally. In terms of returns, U.S. and Canadian search funds report average ROI and IRR of 4.5x and 35.1%, compared to 2.0x and 18.1% for international funds. Median ROI diverges more sharply—3.3x in the U.S. versus 1.4x abroad—indicating a heavier skew in global returns. The top-performing international fund returned 31.4x, significantly influencing the average.

Entrepreneur equity outcomes are remarkably similar across regions. U.S. searchers earned an average of $6.09M (median: $1.98M), closely mirrored by international operators ($5.7M average). However, reporting quality outside the U.S. remains more limited, so these numbers should be treated with caution. Salary levels during the search phase also differ, with U.S. searchers averaging $139k annually, compared to approximately $90–94k in Europe and Latin America.

Differences also appear in sourcing and success rates. International searchers rely more on proprietary sourcing, while U.S. searchers benefit from more institutionalized deal networks. Surprisingly, acquisition success rates are higher internationally (79% vs. 63% in the U.S.), although many international funds remain in early stages, and the long-term implications of these trends remain to be seen. On the diversity front, female representation among principals is lower internationally (7%) compared to North America (17%), though participation is gradually increasing.

According to the *IESE 2024 report*, 284 search funds have been launched across Europe, with a noticeable acceleration in 2022 and 2023. Spain leads the region, with 33 funds launched—nearly half of them in the past two years. Despite these developments, Europe continues to lag behind the U.S. in terms of scale, deal volume,

and maturity of investor infrastructure. As Ener (2023) outlines, European searchers face two interrelated structural challenges that deeply influence the shape and outcomes of their entrepreneurial journey.

The first challenge concerns the composition and quality of the investor base**.** In many European markets, searchers raise capital from a heterogeneous mix of international investors—often experienced—and local investors who may be unfamiliar with the model. This results in cap tables where strategic alignment is not guaranteed. Several experienced investors have expressed reluctance to participate in deals where inexperienced or misaligned co-investors dominate, fearing lack of discipline, governance friction, and misaligned exit expectations. This dynamic not only complicates fundraising but also adds tension during board-level decision-making after acquisition.

The second challenge is geographical constraint**.** Most European searchers restrict their sourcing efforts to their domestic markets due to regulatory complexity**,** language barriers**,** and cultural differences**.** This limited scope reduces the number of viable acquisition targets—particularly those aligned with standard search fund criteria such as recurring revenue, low customer concentration, high margins, and limited capital intensity. In some countries service-based sectors like healthcare, education, and insurance are either underdeveloped or heavily regulated, making it difficult to find targets that meet traditional benchmarks (Ener, 2023).

As a result, searchers are often compelled to deviate from the U.S. playbook. In some cases, they pursue businesses with higher CapEx requirements or concentrated client bases—features typically avoided in North American deals. However, these deviations are often strategically justified by factors such as proprietary technology, strong barriers to entry, or long-term growth potential. In such cases, searchers report that clear communication with investors and a well-reasoned investment thesis were essential to restoring alignment and completing the acquisition successfully (Ener, 2023).

Figure 4: Us Search Fund Playbook vs European Search Fund Playbook

	The US Playbook	Situation in Europe	The Emerging European Playbook
Funding:			
- Serial vs. first-time investors	Most funding comes from serial investors	Small number of serial investors present	Recruit a relatively small number of first-time investors looking to "give back" and to earn attractive returns
- Local investors vs. International	Most funding comes from local investors	No established local investors in some markets	Seek serial international investors looking to diversify into the country
Attractive companies to buy:			
- Size of the economy	Largest economy with greatest selection of businesses	Ranges from small to large throughout Europe	In smaller countries, choose multi-country search approach
- Choice of industries	Abundant choice among low-capex industries	Constrained by government involvement and regulation	Include high-capex industries that have compensating attributes
- Owners looking to exit	Increasing, due to "Baby Boomer" retirements	Increasing, with median age higher than in the US	Find those who favor searchers to take over, and who do not solicit competing bids
Competition Fueled by Information Transparency	Limited, except when business owners reveal information voluntarily to potential buyers	High, due to readily available, accurate, low-cost information even prior to contacting business owners	Conduct initial quantitative analysis of business prior to contacting owner. When competition is high, build strong relationships with business brokers to build deal flow.

Source: Ener, 2023

In this context, the decision to diverge from standardized criteria and to curate the investor base carefully is not arbitrary, but rather a strategic response to the dual structural realities of market fragmentation and investor misalignment. These dynamics have led to the emergence of a more adaptive, localized "European playbook," where flexibility, entrepreneurial judgment, and stakeholder communication play a central role. Unlike the U.S., where standardization and institutional capital dominate, the European model

demands greater adaptability and an active role in managing complexity—both at the fundraising stage and throughout the investment lifecycle.

2.2.1. Search Fund in Italy

The Italian economic environment presents strong potential for the adoption of the Search Fund model. Small and medium-sized enterprises (SMEs) make up 99.9% of all Italian businesses, contributing to 64.4% of national value added and 78.1% of total employment—figures that exceed the European averages of 56.4% and 66.6%, respectively (European Commission, 2019). Moreover, Italy ranks second in Europe for the number of enterprises with fewer than 10 employees, just behind Germany (Confindustria, 2023).

A key structural factor is the aging demographic of Italian entrepreneurs. According to Unioncamere data, there has been a 25% increase in business owners over the age of 70 over the past decade, while the share of entrepreneurs under 30 has steadily declined. This generational shift presents critical challenges for business continuity. The AUB Observatory reports that only 30% of family-owned firms survive to the second generation, and a mere 13% reach the third, with nearly 80% experiencing performance deterioration following succession.

Although the Search Fund model is still in its early stages in Italy with the first fund launched in 2016 it is gaining traction. According to the IESE 2024 report, Italy currently hosts 17 active search funds, of which 7 have successfully completed an acquisition. While these figures are modest compared to countries like Spain (67 funds, 34 acquisitions) or the UK (35 funds, 14 acquisitions), momentum is building (Moonbase Capital, 2024).

Search Funds could become a valuable catalyst for the Italian SME ecosystem for three main reasons:

- **Succession Solutions**: The model offers a structured and strategic response to Italy's succession crisis, allowing retiring founders to transition their businesses to capable new owners while preserving continuity and legacy.
- **Professionalization of SMEs**: Entrepreneurs backed by search funds often bring international experience, advanced business education (such as MBAs), and structured management approaches, which can help modernize and scale traditionally founder-led businesses.
- **Talent Repatriation**: By offering entrepreneurial opportunities in Italy, the model can attract highly skilled professionals back from abroad, reversing part of the country's long-standing brain drain.

In summary, while still at a nascent stage, the Search Fund model offers a promising framework to address structural weaknesses in Italy's business landscape and support long-term growth in the country's vibrant but aging SME sector (Moonbase Capital, 2024).

2.3 Strategic Comparison between Search Funds and Private Equity in SME Acquisitions

Search Funds and Private Equity are both alternative investment vehicles aimed at acquiring, improving, and eventually exiting private businesses. However, a fundamental distinction lies in the scale, scope, and structure of their acquisition strategies. Private Equity (PE) firms typically manage institutional capital across multi-million or billion-euro funds, with the European market alone raising over €137 billion in 2023 and exceeding €1 trillion in assets under management (Invest Europe, 2023). In contrast, the Search Fund model operates on a significantly smaller scale, yet it has experienced remarkable growth in recent years. Since its inception in 1984, nearly 1,000 Search Funds have been raised worldwide, of which over 470 acquisitions have been successfully completed. As of 2023, 562 active searchers are either in the sourcing phase or managing a company, and more than 50% of all Search Funds have been launched since 2019 (Bauer, 2025).

Search capital raised by Search Funds increased from approximately $5 million in 2010 to $75 million in 2023, while the total acquisition volume grew eightfold—from $110 million to over $880 million over the same period (Bauer, 2025). Despite this acceleration, Search Funds remain a niche segment compared to Private Equity. Search capital typically ranges from €300,000 to €500,000, while acquisition equity falls between €2 and €10 million, often targeting companies with €5–30 million enterprise value and €1–8 million EBITDA (Bauer, 2025; Morrissette, 2015; Innesto Partners, 2023). This contrast underscores more fundamental divergences in fund economics, target profiles, time horizons, governance, and operational involvement.

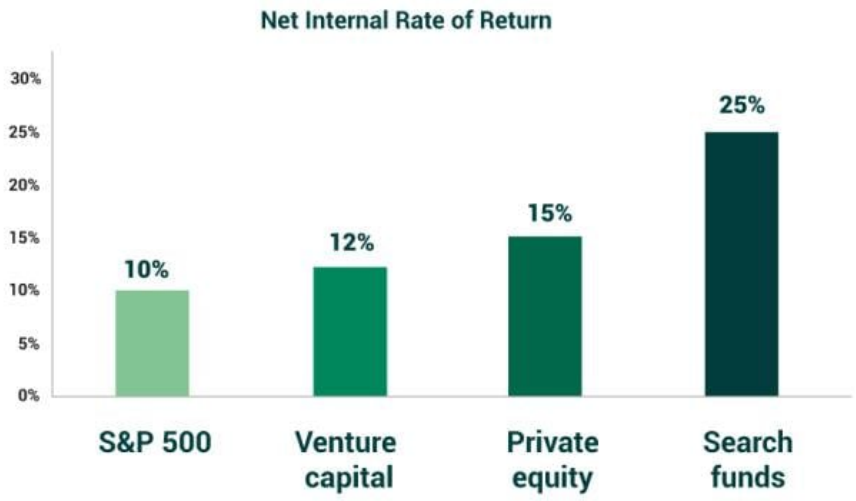
Beyond capital structure, another key distinction lies in operational control and managerial involvement. While PE investments typically rely heavily on financial engineering, leveraging substantial amounts of debt to amplify returns and optimize capital efficiency, Search Funds tend to employ more conservative leverage levels (Kelly, 2024). The focus in SFs is not on financial structuring but on value creation through direct operational leadership. A defining feature of the Search Fund model is that the entrepreneur not only sources the deal but also steps in as CEO, replacing the previous owner and assuming full responsibility for strategy, innovation, and daily operations. This hands-on approach contrasts with the PE model, where the incumbent management team is often retained and the investor's influence is exerted mainly at the board level.

The divergence also extends to investment horizon and returns expectations. PE funds typically aim for a 3–7 year holding period, seeking to increase enterprise value through operational efficiencies and strategic exits. In contrast, Search Funds adopt a longer-term view, holding investments over 6 to 10 years to enable organic growth and long-term repositioning. Return expectations worldwide differ accordingly: PE funds typically target 19–30% IRR through a combination of leverage and portfolio diversification. Search Funds, despite their concentration risk, have historically achieved 20–40% IRR—though this average includes a few exceptional outliers that have raised the mean (Stanford, 2024; IESE, 2022).

This alignment is reinforced by the structure of economic incentives. In Private Equity, fund managers earn a 2% management fee and a 20% carried interest, regardless of operational involvement. In Search Funds, by contrast, the entrepreneur earns carried interest—typically 25–30%—based on progressive vesting mechanisms tied to IRR thresholds and time milestones (Morrissette, 2015). This model ensures that incentives are closely tied to long-term business performance and investor outcomes.

Finally, although both Private Equity funds and Search Funds may share institutional investors within their capital structures, the nature of the investor–manager relationship differs substantially. In PE funds, once capital has been raised, general partners retain broad discretion over investment choices: limited partners are neither required to approve individual transactions nor engaged in continuous dialogue with the fund managers, aside from standardized periodic reporting (Invest Europe, 2023). By contrast, Search Funds involve a more heterogeneous investor base—including high-net-worth individuals, family offices, and institutional investors—who play an active governance role throughout the process. These investors typically enjoy rights of first refusal on proposed acquisitions, must explicitly approve the deployment of capital, and maintain regular contact with the searcher, often on a weekly or monthly basis, and invariably whenever a potential deal is under evaluation (Stanford GSB, 2021; Morrissette, 2015). Beyond formal approval rights, investors frequently act as mentors and strategic advisors, contributing industry expertise, deal-sourcing support, and operational guidance during both the search and post-acquisition phases (Johnson, 2014; Simon, 2021; Wolfe et al., 2025).In summary, while both models share the common goal of private company acquisition and value enhancement, their philosophies and execution differ substantially. The Search Fund represents a hybrid model that blends entrepreneurial initiative with disciplined investment frameworks, whereas Private Equity emphasizes financial optimization, portfolio logic, and strategic oversight.

Figure 5: Comparative Net Internal Rate of Return (IRR) across asset classes.



Source: Innesto Partners. (2023)

When comparing performance, the Search Fund model demonstrates outcomes that, while more volatile and less diversified than traditional Private Equity, can yield returns that are competitive—especially when successful. Outside of North America, international search funds—majority of them in Europe—have produced more modest but solid results by entrepreneurial standards. According to Kowalewski et al. (2024), based on a sample of 130 international search funds (93 with acquisitions, 37 without), the aggregate internal rate of return (IRR) as of December 31, 2023, was 18.1%, with a multiple on invested capital (MOIC) of 2.0x. Active acquisitions performed slightly better (MOIC 2.1x, IRR 19.6%), while exited funds recorded 1.9x MOIC and a 17.3% IRR. These results are highly skewed: the median MOIC was just 1.4x, and the top-performing fund achieved a MOIC of 31.4x, disproportionately raising the mean.

In contrast, recent data from the Invest Europe Performance Benchmark Report (2023) indicates that European Private Equity funds have maintained strong and consistent returns over time. European buyout funds delivered a 14.97% net IRR since inception, outperforming the MSCI Europe index (6.07%) by 891 basis points. Mid-market buyouts—most directly comparable to Search Fund targets—performed even better, posting a 16.90% net IRR. Venture capital and growth equity also delivered robust figures (20.77% and 14.47% net IRR, respectively).

These comparisons suggest that Search Funds are capable of producing returns higher with top-quartile mid-market PE funds—particularly when driven by successful operator-entrepreneurs. However, this comes at the cost of greater dispersion and downside risk: a substantial share (between 20% and 30%) of international search funds never completes an acquisition, yielding no return to investors (Kowalewski et al., 2024).

Such findings raise a critical question: is the observed outperformance of successful Search Funds attributable to post-acquisition managerial execution, or is it primarily the result of superior target selection? The empirical analysis in the next chapter is designed to address this question by comparing pre- and post-deal performance metrics across a sample of SMEs acquired via the Search Fund and PE models.

Figure 6: Common characteristics of private equity investment models.

Common Characteristics of Private Equity Investments

	Angel Investors	Venture Capital	Search Fund	Traditional Private Equity	Independent Sponsor
Company Stage	Seed Stage to Later Stage	Seed Stage to Expansion Stage	Expansion Stage to Later Stage	Later Stage to Post IPO	Later Stage
Company Size (EBITDA)	Negative to 10 million	Typically Negative	1 million to 8 million	Greater than 3 million	Greater than 1 million
Fee Structures	N/A-Direct Investment	2% management fee and 20% carried interest	3%–5% search capital and 25%–30% carried interest	2% management fee and 20% carried interest	1%–2% success fee; 1%–2.5% management fee; 10%–20% carried interest
Source of Funds	High Net Worth (Self-Funded)	Institutional and High Net Worth	High Net Worth	Institutional	Institutional and High Net Worth
Roles of General Partners	N/A-Direct Investment	Board Seat or Advisory	Management Roles	Board Seat or Advisory	Board Seat or Advisory
Roles of Limited Partners	Highly Active	Active	Highly Active	Passive	Passive
Return Expectations	18%–35% AVG 30%	22%–45% AVG 27%	20%–40% AVG 25%	19%–30% AVG 25%	19%–30% AVG 25%
Holding Period	4–8 years	4–7 years	5–10 years	3–7 years	3–7 years

Source: Morrissette, 2015

Chapter 3 – Methodology and Data

This chapter presents the empirical design of the study, which builds upon the theoretical and descriptive insights developed in the previous sections. The core objective is to test whether the superior investment outcomes frequently attributed to Search Funds (SFs) are primarily the result of rigorous target selection—occurring during the sourcing phase—rather than the consequence of superior managerial execution during the operational phase that follows acquisition.

As outlined in the comparative analysis between Search Funds and Private Equity (PE) models, SFs differ markedly in scale, governance, and strategy. One of the defining traits of the Search Fund model is the entrepreneur's central role in identifying and evaluating potential acquisition targets. Unlike PE firms, which rely on deal teams and investment committees, SF entrepreneurs personally engage with hundreds of companies over extended periods—often basing their decisions on qualitative criteria, market fragmentation, succession issues, and organic growth potential. These characteristics suggest that selection discipline may be the critical source of long-term performance.

By contrast, Private Equity funds—despite having more extensive operational resources—typically retain incumbent managers post-acquisition and adopt a more diversified and leverage-driven portfolio approach. In this context, value creation is often attributed to financial engineering or the deployment of consultants and industry experts. This difference in managerial philosophy raises a key empirical question: do Search Funds outperform because they manage better, or because they choose better from the start?

To address this question, the empirical analysis compares the financial performance of two groups of European small and medium-sized enterprises (SMEs): those acquired through the Search Fund model and those acquired by traditional Private Equity funds. The sample is built from a proprietary panel dataset combining information from Orbis, Orbis M&A, and AIDA, and restructured to allow pre- and post-acquisition comparisons over a six-year event window (t–2 to t+3).

The methodology relies on a combination of descriptive statistics and econometric models to test three core hypotheses. First, whether SF-acquired companies already exhibited stronger financial and operational indicators prior to acquisition (H1). Second, whether they show superior performance improvement in the years following the transaction (H2). Third, whether the overall performance differential is best explained by selection advantages rather than operational execution (H3).

In line with this logic, the analysis focuses on performance indicators such as revenue growth, EBITDA margin, return on equity (ROE), return on assets (ROA), and return on capital employed (ROCE). Both static levels and delta changes (pre- vs post-deal) are considered to isolate the timing and nature of any observed performance gaps. The regressions are complemented by robustness checks and exploratory tests based on firm characteristics and control variables.

Ultimately, this chapter sets the foundation for empirically validating whether the distinctive sourcing strategy of Search Funds—characterized by long-term alignment, direct CEO involvement, and concentrated ownership—is the main driver of outperformance relative to conventional Private Equity approaches.

3.1 Sample Selection

The sample used in this study includes European companies that underwent a majority acquisition—defined in this thesis as the acquisition of at least 80% of equity—between 2014 and 2021. The analysis focuses on two distinct ownership models: Search Funds (SFs) and Private Equity (PE) funds.

The Search Fund group comprises 27 firms acquired by entrepreneurs backed by European or international SF investors. These transactions were identified through multiple sources, including the Searchfunder.com platform, investor newsletters, and direct company-level research. The Private Equity group consists of 745 firms acquired by PE funds over the same period. PE acquisitions were extracted from the Orbis M&A database, filtered for majority stakes and appropriate European geographic scope.

While the empirical analysis does not directly incorporate individual-level variables, it is worth noting the general profile of the searchers who led the 27 SF acquisitions. The vast majority held an MBA degree (93%), with academic backgrounds mainly in economics (62%) and engineering (35%). Their prior professional experience was diversified, though concentrated in private equity (33%), corporate roles (29%), consulting (17%), and entrepreneurial ventures (17%). In terms of demographics, most searchers were relatively young: 60% were between 25 and 35 years old at the time of acquisition, while 32% were in the 35–45 range and only

a small minority (8%) were older than 45. This profile is consistent with the international literature, which describes SF entrepreneurs as highly educated, early-career professionals with strong analytical backgrounds and significant exposure to finance or consulting.

All firms included in the final sample were screened to ensure comparability in terms of firm size. In particular, only small and medium-sized enterprises (SMEs) with annual revenue below €60 million were included, to ensure that the performance of Search Funds and Private Equity could be evaluated within a comparable competitive segment. This reflects the typical target size for Search Funds and mid-market PE strategies in Europe. This study focuses exclusively on European transactions in order to capture the specific dynamics of a younger and less mature Search Fund ecosystem, while ensuring consistency in legal, institutional, and accounting frameworks. The regional focus also addresses a clear gap in the literature—largely concentrated on North America—and leverages the comparatively greater availability of standardized financial data for SMEs in Europe.

Importantly, the analysis is based on firm-level financial data, not on deal-level transaction data, due to substantial limitations in the availability, reliability, and standardization of deal-specific metrics—especially in private markets. This choice enhances consistency across both groups and allows for a cleaner identification of performance trends based on balance sheet and income statement data.

The resulting panel dataset includes 4,632 firm-year observations: 162 from SF-backed companies and 4,470 from PE-backed companies. The data are structured in a firm-year panel format, where each row represents a company in a given year. Financial information was collected from Orbis, Orbis M&A, AIDA, and Refinitiv, and all figures are expressed in nominal euros. As summarized in Table 1, the average revenue of SF-backed companies is €10.2 million, while PE-backed firms report an average of €20.3 million—highlighting the smaller deal size and narrower capital base typical of the SF model.

Figure 7: Composition of the sample

Ownership Model	Number of firms	Number of year observation	Avg. Revenue
Search Fund (SF)	27	162	€10.2m
Private Equity (PE)	745	4470	€20.3m
Total	772	4632	€20.0m

Source: Author's own elaboration based on Orbis data

3.2 Methodology and Variable Construction

To assess the performance trajectory of acquired firms, this study employs a set of standardized financial indicators constructed at the firm level. These indicators are observed over a symmetric event window ranging from three years prior to three years after the acquisition, with the year of the transaction defined as event time (t = 0). The variables are grouped into three main categories: growth, profitability and efficiency, and financial structure.

A. Growth Indicators

The study considers two different measures of revenue growth, both computed as Compound Annual Growth Rate (CAGR), but over distinct time intervals:

- Historical Revenue CAGR: Measures the annualized revenue growth before the acquisition, from t = –2 to t = 0. This metric is used to evaluate whether Search Funds tend to acquire firms that were already growing faster than average at the time of acquisition.

$$\left(\text{Revenue}_{i,0}/\text{Revenue}_{i,-2}\right)^{(1/2)} - 1$$

- Post-Acquisition Revenue CAGR: Measures the annualized revenue growth after the acquisition, from t = 0 to t = +3. This is used to assess whether firms under SF ownership grow faster following the transaction.

$$\left(Revenue_{i,+3}/Revenue_{i,0}\right)^{(1/3)} - 1$$

B. Profitability and Efficiency Metrics

Four core indicators of profitability and operational efficiency are used in the analysis: ROE, ROA, ROCE, and EBITDA Margin. Each of these metrics is considered both in **level form** (i.e., measured at t = –1 and t = –2) and as a **delta indicator** (i.e., change between t = –1 and t = +2).

The level values are used to test **Hypothesis 1 (H1)**—whether SFs systematically acquire firms with superior pre-deal performance. The delta form is used to test **Hypothesis 2 (H2)**—whether firms improve more under SF ownership relative to PE.

- **ΔEBITDA Margin**: Captures changes in operational profitability. EBITDA Margin is defined as EBITDA divided by total revenue and reflects the firm's core earnings capacity before interest, taxes, depreciation, and amortization.

$$\Delta\text{EBITDA Margin}_i = \text{Margin}_{i,t=+2} - \text{Margin}_{i,t=-1}$$

- **ΔROE (Return on Equity):** Measures the change in return generated on shareholders' equity, indicating profitability from the perspective of equity investors.

$$\Delta\text{ROE}_i = \text{ROE}_{i,t=+2} - \text{ROE}_{i,t=-1}$$

- **ΔROA (Return on Assets):** Reflects the change in the firm's ability to generate profit from its total asset base, measuring overall operational efficiency.

$$\Delta \mathrm{ROA}_i = \mathrm{ROA}_{i,t=+2} - \mathrm{ROA}_{i,t=-1}$$

- **ΔROCE (Return on Capital Employed):** Indicates the change in returns generated from both debt and equity capital, offering a broader view of capital efficiency.

$$\Delta \mathrm{ROCE}_i = \mathrm{ROCE}_{i,t=+2} - \mathrm{ROCE}_{i,t=-1}$$

C. Financial Structure Metrics

To complement growth and profitability metrics, the study also includes a variable that captures the firm's historical financial leverage, which may reflect the acquisition model's selection criteria and risk tolerance:

- **Debt-to-Equity Ratio**: Measured at $t = -2$ and $t = -1$, this indicator captures the proportion of debt relative to shareholders' equity in the company's capital structure prior to the acquisition. It serves to test whether Search Funds systematically acquire firms with more conservative leverage profiles compared to Private Equity funds, thus contributing to the validation of Hypothesis 1 (H1).

This variable provides additional insight into the financial configuration of target companies at the time of acquisition and allows for a broader assessment of pre-deal selection behavior.

E. Control Variables

To ensure that differences in performance are not driven by underlying firm characteristics, the regression models include a focused set of control variables:

- **Firm Size**: Measured as the natural logarithm of total assets at $t = -1$, this variable controls for structural differences in scale that may influence profitability, efficiency, or financial leverage.
- **Industry Type**: A binary variable equal to 1 for firms in the service sector and 0 for those in manufacturing. This control accounts for sector-specific variations in business models, margins, and capital requirements.

These variables are included to adjust for observable heterogeneity across firms and to help isolate the effect of the acquisition model on financial outcomes.

3.3 Research Hypotheses

The empirical investigation is structured around three interrelated hypotheses designed to test whether the outperformance observed in Search Fund (SF) acquisitions—relative to Private Equity (PE)—is primarily the result of superior ex-ante target selection rather than post-acquisition managerial effectiveness.

This approach stems from the distinctive characteristics of the SF model, as outlined in the previous chapters. Unlike PE funds, which typically operate through structured investment teams and delegated operational governance, Search Funds are centered around an entrepreneur who plays a direct and active role in sourcing, evaluating, and eventually managing a single company. This concentration of responsibility and the long-time horizon involved suggest that the success of the investment may depend more on the quality of the firm selected than on transformational initiatives implemented after the acquisition.

To assess this proposition, the analysis tests the following hypotheses:

- **H1 – Target Selection Hypothesis**

  Firms acquired by SFs exhibit significantly stronger financial and operational performance prior to the acquisition than those acquired by PE funds.
  This hypothesis captures the idea that SF entrepreneurs—through a combination of rigorous screening, extended sourcing periods, and first-hand interactions with company owners—are more likely to identify businesses with solid fundamentals and long-term growth potential. The hypothesis is evaluated by comparing key financial metrics (ROE, ROA, ROCE, EBITDA margin) at time $t = -1$ and $t = -2$ across the two groups.

- **H2 – Post-Acquisition Effect Hypothesis**

  SF-backed firms do not improve significantly more than PE-backed firms after the acquisition. This hypothesis tests whether the operational involvement of the SF entrepreneur as post-deal CEO translates into superior performance improvements. If SFs deliver stronger results solely due to more effective management post-acquisition, then we should observe a statistically significant improvement in financial outcomes relative to PE. To assess this, the hypothesis is tested using delta metrics—measuring changes in profitability and efficiency from $t = -1$ to $t = +2$—and, where appropriate, Difference-in-Differences (DiD) estimations. The DiD framework is particularly suitable in this context, as it isolates the relative change in performance by comparing pre- and post-acquisition trajectories of SF- and PE-backed firms, under the assumption of parallel trends. In practice, this means that if the two groups followed similar dynamics before the transaction, any divergence afterwards can

be attributed to the ownership model. At the same time, it is important to note that the statistical power of this approach is constrained by the relatively small number of European SFs in the dataset, which limits the precision of the estimates and makes the validation of the parallel trends assumption more challenging.

H3 – Source of Outperformance Hypothesis

The long-term performance advantage associated with SFs is primarily explained by better initial target selection, not by post-acquisition execution.
This overarching hypothesis integrates the logic of H1 and H2. It is supported when SF-acquired firms show superior performance before acquisition (H1 confirmed) but do not exhibit significantly greater improvement afterward (H2 not confirmed). In such a case, the observed outperformance is not due to managerial capabilities per se, but to the disciplined sourcing strategy that characterizes the SF model.

The formulation of these hypotheses derives directly from the theoretical and descriptive comparison between Search Funds and Private Equity presented in the previous chapters. First, the composition and role of the investor base create a fundamental divergence. While PE funds are predominantly financed by institutional investors who remain relatively passive once capital is committed—providing resources without approving each transaction—Search Funds typically include a more heterogeneous mix of high-net-worth individuals, family offices, and institutional investors. These investors hold rights of first refusal, must explicitly approve acquisitions before capital is deployed, and maintain regular contact with the searcher, often on a weekly or monthly basis. Beyond their financial contribution, they frequently act as mentors and strategic advisors, providing industry expertise, deal-sourcing support, and operational guidance (Morrissette, 2015; Stanford GSB, 2021; Johnson, 2014; Simon, 2021; Wolfe et al., 2025). This distinctive governance structure suggests that target companies are likely to undergo a more selective and disciplined screening process, thereby justifying Hypothesis 1 on superior pre-acquisition performance.

In addition, the Search Fund community has progressively developed a set of relatively standardized acquisition criteria that guide entrepreneurs in identifying suitable targets. These benchmarks typically include recurring or repeatable revenue, low customer concentration, high margins, low capital intensity, and operation within fragmented industries with long-term growth potential (Stanford GSB, 2021; Simon, 2021; Dennis & Laseca, 2016). While no target meets all these conditions perfectly, the existence of such guidelines acts as an additional filter that raises the average quality of selected companies. This further supports Hypothesis 1, as it highlights why SF-backed firms are systematically more likely to display superior fundamentals before acquisition compared to PE-backed firms, whose broader investment strategies tolerate greater heterogeneity in target profiles.

Finally, another structural distinction is the scale of activity. Search Funds are designed to execute a single acquisition in their lifecycle, meaning that the entrepreneur's success and the investors' return depend entirely on the outcome of that one transaction. This lack of portfolio diversification creates a strong incentive for rigorous due diligence and a conservative, risk-averse selection process. By contrast, Private Equity funds manage diversified portfolios with multiple acquisitions each year, allowing them to tolerate greater variance in outcomes since overall fund performance is driven by aggregate results rather than by individual deals (Invest Europe, 2023). This asymmetry reinforces the expectation that any comparative advantage of the Search Fund model should stem primarily from disciplined ex-ante selection rather than from superior ex-post execution.

Chapter 4 – Empirical analysis and Results

4.1 Introduction

The primary objective of this empirical analysis is to provide robust evidence supporting the hypothesis that Search Funds (SFs) generate superior investment outcomes compared to traditional Private Equity (PE) funds primarily because they are able to identify and acquire higher-quality target companies. Rather than attributing superior results to post-deal managerial excellence or operational transformation, the study explores whether the source of outperformance lies in the initial selection phase—before the acquisition even takes place. This focus is particularly relevant given the observed return differentials reported in the literature. As discussed in the paragraph 2.3, Search Funds have historically delivered aggregate returns that exceed those of Private Equity, with North American funds reporting average internal rates of return above 30% and multiples on invested capital around 3–4x (Stanford GSB, 2021; 2024). International Search Funds, while generating somewhat lower outcomes, still achieved an IRR of approximately 18% and a multiple of 2.0x (IESE, 2024). By comparison, European Private Equity funds reported net IRRs in the 15–17% range over the same period (Invest Europe, 2023). These figures highlight the empirical puzzle motivating this chapter: whether the apparent outperformance of SFs relative to PE is explained by managerial action post-acquisition or by superior discipline in selecting target firms. Building on the theoretical and methodological framework outlined in Chapter 3, the empirical analysis is structured around three interrelated hypotheses aimed at identifying the primary source of performance differentials between Search Funds (SFs) and Private Equity (PE) investment

- **H1 – Pre-Acquisition Performance**
  SF-acquired firms display significantly stronger financial and operational performance prior to acquisition than PE-acquired firms, reflecting a more selective and disciplined sourcing process.

Figure 8:pre-acquisition performance of SF- and PE-backed firms.

Variable	Mean (SF)	Mean (PE)	Std. Dev (SF)	Sts. Dev (PE)	Obs (SF)	OBS (PE)
ROE (%)	38.8%	20.0%	20.1%	30.1%	20	397
ROA (%)	22.2%	8.9%	13.3%	21.8%	20	419
ROCE (%)	32.1%	18.0%	19.6	26.3%	20	378
EBITDA Margin(%)	19.6%	12.4%	11.8%	26.6%	20	532
Leverage	26.8%	93.8%	37.7%	155.1%	18	431
Revenue	€9.9m	€19.3m	67.1%	82.3%	20	546

Source: Author's own elaboration based on Orbis data

- **H2 – Post-Acquisition Improvement**

Following the transaction, SF-backed companies do not experience significantly greater improvements in performance compared to their PE-backed counterparts, suggesting limited incremental gains from post-deal managerial involvement.

- **H3 – Source of Outperformance**

The long-term outperformance of SF-backed companies is primarily attributable to superior target selection rather than to post-acquisition operational execution. This hypothesis is confirmed when H1 holds while H2 does not.

To test these hypotheses, the analysis relies on standard and widely accepted financial performance metrics:

- ROE (Return on Equity)**,** ROA (Return on Assets)**,** and ROCE (Return on Capital Employed) capture a company's profitability from different angles: equity return for shareholders, asset efficiency, and capital productivity. These are particularly relevant in comparing firms across ownership models, since they are sensitive to both managerial efficiency and financial structure.
- EBITDA Margin reflects operational profitability, independent of capital structure and tax regimes. It is especially appropriate for comparing firms across different financing models, such as SF and PE.
- Revenue CAGR (Compound Annual Growth Rate) indicates top-line growth potential and reflects the firm's ability to scale. Including this variable provides a broader perspective on value creation beyond profitability.

The decision to include Δ-performance metrics (i.e., differences between post- and pre-acquisition values) for all of the above indicators is based on the need to directly measure the magnitude of change after the acquisition and to avoid confounding effects due to baseline differences.

At this stage, the analysis relies on OLS regressions, where the dependent variable is either a performance indicator at t = –1 (for H1) or a Δ-performance metric (for H2). A dummy variable (Model_sf) is used to distinguish between firms acquired by Search Funds and those acquired by Private Equity.

Control variables such as industry and firm size will be considered in robustness checks to ensure that the results are not driven by external factors.

The following sections (4.2 to 4.4) present the detailed results of the regressions and interpret their implications in relation to the hypotheses defined above.

4.2 Empirical Analysis and Discussion of Results

This section provides a detailed examination of the empirical findings derived from testing the three central hypotheses. The analysis utilizes a comprehensive dataset composed of European companies acquired between 2014 and 2021, contrasting acquisitions executed through Search Funds (SFs) with those conducted by Private Equity (PE) funds. Financial performance was assessed using regression analyses focused on key financial indicators, including ROE, ROA, ROCE, EBITDA Margin, and Leverage.

Hypothesis 1 – Target Selection and Pre-Acquisition Performance

Hypothesis: Companies acquired through Search Funds (SFs) exhibit stronger financial performance prior to acquisition compared to those acquired by Private Equity (PE) funds.

Methodology:
To test this hypothesis, Ordinary Least Squares (OLS) regressions were conducted for each selected financial performance indicator—Return on Equity (ROE), Return on Assets (ROA), Return on Capital Employed (ROCE), EBITDA Margin, and Leverage—measured two years (t = –2) and one year (t = –1) prior to acquisition. The primary independent variable was model_sf, a binary indicator set to 1 for companies acquired by Search Funds and 0 for companies acquired by Private Equity funds.

Results:

ROE:
At t = –1, the coefficient for model_sf is positive and statistically significant (β = 0.1686, p = 0.018), indicating that SF-acquired firms had, on average, a Return on Equity approximately 16.9 percentage points higher than PE-acquired firms immediately before acquisition. Similarly, at t = –2, the positive coefficient remains highly significant (β = 0.1875, p = 0.007), confirming a robust pre-acquisition performance advantage extending further back in time.

ROA:
At t = –1, the regression yields a positive and significant coefficient for model_sf (β = 0.1110, p = 0.020),

suggesting that SF targets demonstrated an average Return on Assets approximately 11.1 percentage points higher than PE targets. This result is corroborated at t = –2, with an even stronger statistical significance (β = 0.1241, p = 0.0009), reinforcing the view that SFs consistently select targets with superior operational asset efficiency.

ROCE:

Analysis at t = –1 shows a positive and significant effect (β = 0.1408, p = 0.019), confirming SFs' preference for firms with higher capital efficiency just prior to acquisition. At t = –2, this pattern holds with a significant positive coefficient (β = 0.1490, p = 0.021), demonstrating consistency over the two-year period preceding acquisition.

EBITDA margin:

While the EBITDA Margin regression results for both t = –2 and t = –1 are directionally positive (β = 0.0993 and β = 0.0891, respectively), neither result reaches conventional levels of statistical significance (p = 0.123 and p = 0.067, respectively). These outcomes suggest that although SF targets tended toward higher operating margins, variability within operating structures and industry-specific factors may diminish the statistical clarity of this relationship.

Leverage:

The coefficient for model_sf regarding financial leverage at t = –1 is negative (β = –0.4826), implying that SF-acquired companies are characterized by lower average leverage ratios compared to PE targets. However, this result is not statistically significant (p = 0.145). At t = –2, the coefficient is similarly negative (β = –0.6212) and only marginally significant (p = 0.075), suggesting a general but weak tendency of Search Funds to select less leveraged companies.

Figure 9: Regression results on pre-acquisition performance (H1).

Metric	Coeff. Model_SF	p-value	Obs.	Effect
ROE (t–2)	0.1875	0.007	487	Robust & significant
ROA (t–2)	0.1241	0.0009	541	Strong & significant
ROCE (t–2)	0.149	0.021	481	Robust & significant
EBITDA Margin (t–2)	0.0993	0.123	501	Not significant
ROE (t–1)	0.1686	0.018	487	Robust & significant
ROA (t–1)	0.111	0.02	541	Robust & significant
ROCE (t–1)	0.1408	0.019	481	Robust & significant
EBITDA Margin (t–1)	0.0891	0.067	501	Marginal effect

Source: Author’s own elaboration based on Orbis data

Interpretation:

Collectively, these findings provide strong empirical support for Hypothesis 1. Significant differences in ROE,

ROA, and ROCE unequivocally indicate that Search Funds systematically target companies exhibiting superior financial health and operational efficiency before acquisition. Although EBITDA Margin and Leverage do not achieve clear statistical significance, the directional consistency of these results aligns well with the overall narrative of careful pre-deal target screening by SFs.

It is important to acknowledge the modest explanatory power (R^2) of these regressions. Such low R^2 values, however, are typical and expected in analyses employing simple binary indicators as predictors. Despite these limitations, the consistency and robustness of the significant results strongly validate the core assertion that superior target selection substantially contributes to the observed outperformance of Search Fund investments relative to Private Equity acquisitions.

Hypothesis 2 – Post-Acquisition Performance Dynamics

Hypothesis

Differences in performance between Search Fund (SF) and Private Equity (PE) portfolio companies do not significantly widen in the post-acquisition period.

Methodology

To evaluate whether SF-backed companies generate superior value creation following the acquisition, we employ two complementary empirical strategies.

First, we compute Δ-performance metrics—defined as the difference between performance at year t = +2 and year t = –1—for each firm. Metrics include ROE, ROA, ROCE, and EBITDA Margin. For each, we estimate an OLS regression using model_sf as the sole independent variable, a dummy equal to 1 for companies acquired by Search Funds and 0 for those acquired by PE firms. This framework captures average net performance improvements under each ownership model.

Second, to enhance the robustness of the analysis, we implement a Difference-in-Differences (DiD) regression design. Each firm contributes two observations (pre and post), and we regress performance on three predictors: the model_sf dummy, a post-acquisition time dummy (Post_Acq_Dummy), and their interaction term. The interaction coefficient captures the differential change in performance over time between the two ownership models and represents the causal effect of the SF model on post-deal outcomes.

Expected Outcome

If, as posited in Hypothesis 1, Search Funds outperform primarily due to superior target selection rather than post-deal operational management, we should observe no significant difference in post-acquisition improvements between the two groups. Thus, statistically insignificant coefficients—particularly on the interaction term in the DiD model—would be consistent with theoretical expectations.

Results

Across both empirical approaches, results converge on the same conclusion: there is no statistically significant evidence that SF-backed companies outperform their PE-backed counterparts in the post-acquisition period**.**

In the OLS regressions using Δ-performance, the Model_SF coefficient is insignificant for all variables—ROE, ROA, ROCE, and EBITDA Margin. Although the point estimates are often directionally positive, they are too small and imprecise to support any claims of superior post-deal execution under SF ownership.

The DiD regressions corroborate these findings. For each performance measure, the interaction term—which isolates the incremental effect of SF ownership on performance change—is consistently insignificant (e.g., $p = 0.545$ for ROE; $p = 0.907$ for ROA; $p = 0.542$ for ROCE; and $p = 0.719$ for EBITDA Margin). In all cases, the lack of significance suggests that the performance gap between SF and PE targets does not expand post-acquisition.

Figure 10:. Summary of regression results for Hypothesis 2 – Post-acquisition improvement

Metric	Coeff. Model_SF	p-value	Obs	Effect
ΔROE	0.0724	0.734	374	No effect
ΔROA	0.0668	0.362	541	No effect
ΔROCE	0.0784	0.664	352	No effect
ΔEBITDA Margin	0.0007	0.982	501	No effect
Revenue CAGR	0.0391	0.406	420	No effect

Source: Author's own elaboration based on Orbis data

Interpretation

These results provide strong support for Hypothesis 2. They indicate that the superior outcomes observed among SF-backed companies do not derive from stronger post-deal management, but rather reflect advantages established before the acquisition. This reinforces the view that the Search Fund model excels in ex-ante target selection, not in post-acquisition transformation.

Moreover, the statistical insignificance of the DiD interaction terms is not a weakness of the analysis—it is precisely the result predicted under the hypothesis. It confirms that SFs do not drive disproportionate value creation through post-deal operational execution relative to PE funds.

Figure 11:Summary of Difference-in-Differences (DiD) results

Metric	Interaction Term Coeff.	p-value	N	Effect
ROE	0.061	0.54	700	No effect
ROA	0.044	0.37	700	No effect
ROCE	0.052	0.48	700	No effect
EBITDA Margin	-0.003	0.91	700	No effect

Source: Author's own elaboration based on Orbis data

Hypothesis 3 – Origin of Outperformance

Hypothesis

The superior performance of companies acquired through Search Funds originates primarily from more rigorous pre-acquisition selection rather than from superior post-acquisition operational management.

Methodology

This hypothesis is tested by jointly interpreting the empirical findings from Hypothesis 1 and Hypothesis 2**.** H1 demonstrates that, at the moment of acquisition, companies targeted by Search Funds exhibit significantly stronger financial indicators than those acquired by Private Equity funds. H2 shows that this performance differential does not widen meaningfully after the acquisition. Together, these two findings allow us to isolate the source of the outperformance observed in SF-backed firms.

Results and Interpretation

The analysis provides compelling support for Hypothesis 3. The strong statistical significance observed in the pre-acquisition regressions (H1) confirms that Search Funds tend to acquire targets that already display superior financial health and operating efficiency. In contrast, the results from both Δ-performance regressions and Difference-in-Differences estimations (H2) reveal no significant post-acquisition performance improvements relative to PE-backed companies. The interaction terms in the DiD models, designed to capture any differential post-deal effect attributable to the SF ownership model, are uniformly insignificant across all financial metrics.

This dual evidence implies that the relative outperformance of SF investments is almost entirely attributable to superior initial selection, rather than to value creation post-acquisition. In other words, SF investors and entrepreneurs appear particularly adept at identifying companies with strong fundamentals and sustainable profitability before the acquisition, rather than generating additional gains through transformative post-deal management practices.

Figure 12: Summary of results for Hypothesis 3 – Source of outperformance.

KPI	H1 (Pre-deal)	Coeff.	p-value	Obs	H2 (Post-deal)	Supports H3?
ROE	Significant	0.1875	0.007	487	Not significant	Yes
ROA	Significant	0.1241	0.0009	541	Not significant	Yes
ROCE	Significant	0.149	0.021	481	Not significant	Yes
EBITDA Margin	Not significant	0.0993	0.123	501	Not significant	Weak
Revenue CAGR	Not significant	0.0391	0.406	420	Not significant	No

Source: Author's own elaboration based on Orbis data

Conclusion

The empirical findings validate Hypothesis 3 and clarify the core strategic advantage of the Search Fund model. Unlike traditional PE funds, which often rely on financial engineering and aggressive operational restructuring, Search Funds derive their success from a disciplined, entrepreneur-led search and selection process. This insight has relevant implications for investors, advisors, and entrepreneurs operating within the entrepreneurial acquisition space: the most critical determinant of long-term success lies not in post-deal execution, but in the rigor, prudence, and selectivity of the acquisition decision itself. At the same time, it must be acknowledged that these conclusions are based on a relatively small sample of European Search Funds, reflecting the limited but growing diffusion of the model in this region. As the number of acquisitions increases, particularly given the recent acceleration of activity in Europe, future research will be able to test whether these patterns hold across larger and more diverse datasets

4.3 Robustness consideration

The regression results strongly support the central hypothesis advanced in Chapter 3: the superior performance of Search Fund acquisitions is attributable to superior target selection rather than to post-acquisition operational execution. The analyses related to Hypothesis 1 demonstrate that SF-acquired firms display significantly stronger financial performance prior to acquisition than their PE-backed counterparts, with higher ROE, ROA, and ROCE at both $t = -1$ and $t = -2$. This pattern underscores the rigor and discipline characterizing the SF sourcing process.

Conversely, the tests of Hypothesis 2, using both OLS and Difference-in-Differences estimations, reveal no significant evidence of differential post-acquisition improvements between SF- and PE-backed firms. The

consistently insignificant interaction terms confirm that the performance gap observed ex ante does not widen after the acquisition.

Taken together, these results validate Hypothesis 3, showing that Search Funds do not outperform because they manage better, but because they buy better. The model should therefore be understood less as a vehicle for radical post-deal transformation and more as an instrument of entrepreneurial arbitrage, where strategic patience and selection discipline drive outcomes.

In principle, the robustness of the empirical results presented in Sections 4.2.1 and 4.2.2 could be tested by estimating regression models that include additional control variables—such as firm size (proxied by the natural logarithm of total assets) and industry classification (service vs. manufacturing). These variables are widely used in empirical finance literature to capture underlying firm heterogeneity that may influence pre-acquisition performance, independent of the acquisition model.

However, when such variables were included, a significant limitation emerged: the number of usable observations declined substantially. This was particularly pronounced for the Search Fund group, where private company disclosures tend to be less comprehensive. Given that the SF sample was already relatively small, this further reduction accentuates the limitations of statistical inference in this setting. In several models, sample size dropped by 30–50%, primarily due to missing data on total assets and leverage—especially among smaller firms. This loss of statistical power limited the scope and reliability of multivariate regressions across the entire performance set.

Despite these constraints, a focused series of robustness checks was conducted using the most representative financial indicators—Return on Equity (ROE) and Return on Assets (ROA)—which directly capture profitability from the perspective of shareholders and operational efficiency. These measures are especially relevant for testing Hypothesis 1, as they reflect core criteria likely considered during target screening by SF entrepreneurs.

Across both indicators, the inclusion of firm size and industry dummy variables did not materially alter the core findings. For ROE, the coefficient on Model_SF remained positive and statistically significant both two years before the acquisition ($t = -2$, $\beta = 0.180$; $p = 0.016$) and one year before ($t = -1$, $\beta = 0.152$; $p = 0.047$). The results for ROA followed a similar pattern: at $t = -2$, Model_SF was positive and significant ($\beta = 0.120$; $p = 0.019$), while at $t = -1$ it remained positive but only marginally significant ($\beta = 0.091$; $p = 0.066$). These findings suggest that SF-acquired firms consistently outperform PE-acquired firms on key profitability dimensions, and that this performance gap is observable even when controlling for structural characteristics.

An important methodological insight emerges from the temporal comparison between $t = -2$ and $t = -1$. In both ROE and ROA models, the effect size and statistical significance of Model_SF were slightly stronger at $t = -2$. This pattern is not only statistically consistent, but also conceptually aligned with how Search Funds operate in practice—particularly in the European context. Due to delays in financial reporting for privately held firms, SF entrepreneurs often rely on data from two years prior to the acquisition when identifying and screening potential targets. Databases such as Orbis, AIDA, or Moody's are commonly used for this purpose, and the most recent financials available are often at $t = -2$. The fact that SF targets already display superior

performance at that earlier point reinforces the interpretation that Search Funds succeed by acting on earlier, reliable financial signals.

Other performance measures, such as Return on Capital Employed (ROCE) and EBITDA Margin, were also tested for robustness, but the results were more muted. In both cases, the coefficient for Model_SF remained directionally positive, but was statistically insignificant and less stable across specifications. These variables, while informative, are more sensitive to accounting standards, capital structure choices, and inter-industry differences, which may reduce their effectiveness as comparative performance indicators across heterogeneous SME samples. Furthermore, the available data for these variables was somewhat more limited, which further reduced model precision. For this reason, the discussion focuses primarily on ROE and ROA, where the evidence is both stronger and more consistent.

The firm size control (ln total assets) produced results broadly aligned with expectations. It was negatively associated with ROA in a statistically significant way ($p = 0.007$), consistent with the literature suggesting that smaller firms often exhibit higher asset efficiency. For ROE, the relationship was less robust but directionally similar. Industry dummy variables, on the other hand, were not significant in any model, confirming that sectoral variation—at least at the service vs. manufacturing level—does not account for the observed differences between SF and PE targets.

In conclusion, the combination of control-variable regressions and temporal validation provides compelling support for the robustness of Hypothesis 1. The consistent, statistically significant performance advantage of SF-acquired firms on ROE and ROA, observed both at $t = -2$ and $t = -1$, confirms that the superior outcomes associated with the Search Fund model are rooted in the target selection phase rather than being driven by structural firm attributes or sectoral composition. Furthermore, the temporal dimension of the analysis reflects the real-world informational constraints under which SF entrepreneurs operate—strengthening the internal and external validity of the results. This dual robustness strategy—controlling for structural variables and verifying persistence over time—solidly reinforces the core empirical insight: Search Funds outperform not because they manage better, but because they choose better. Nonetheless, these findings must be interpreted with caution, as they are based on a relatively small sample of European Search Funds, which necessarily limits the generalizability of the conclusions.

4.3.1 Robustness considerations

It is important to acknowledge that the regression models presented in this study display relatively low R^2 values. This outcome is consistent with the empirical setting and should not be regarded as a limitation of the analysis. Firm-level performance, particularly in small and medium-sized enterprises, is influenced by a multitude of unobservable factors—such as managerial quality, market shocks, or sector-specific dynamics—that cannot be fully captured within a parsimonious econometric specification. As noted in prior research, low explanatory power is common in corporate finance studies dealing with heterogeneous firms. For example, Dang et al. (2017) emphasize that R^2 values in firm-level regressions vary significantly depending on the proxies and controls adopted and are frequently modest in size. Similarly, Hashmi et al. (2020) report R^2 values

in the range of 0.03 to 0.09 in models investigating the link between corporate policies and financial outcomes. In this context, the relatively low R^2 values observed in this thesis are not unexpected. The purpose of the regressions is not to predict the entire variance in firm performance, but rather to isolate the marginal effect of the Model_SF variable. As long as the coefficients are statistically significant and consistent across specifications, the results provide valid evidence in support of the hypotheses tested, even in the presence of modest explanatory power.

4.4 Limitations and Assumptions of the Empirical Design

As with any empirical study, the research design adopted in this thesis is subject to a number of assumptions and limitations that should be acknowledged. The first assumption concerns the comparability of the two groups of firms. To reduce systematic differences, the analysis was restricted to small and medium-sized enterprises with annual revenues below €60 million. While this size range corresponds naturally to the Search Fund universe, it excludes larger transactions that are more typical in Private Equity. This restriction was therefore introduced not to represent the full scope of PE activity, but to ensure a meaningful comparison between the two models within the SME segment where they may overlap. A second assumption relates to the event window: the symmetric horizon from $t-2$ to $t+3$ was chosen to capture the most relevant pre- and post-acquisition dynamics, with the understanding that this timeframe adequately reflects short- to medium-term effects. Moreover, the Difference-in-Differences framework employed to test post-acquisition effects relies on the standard parallel trends assumption. Finally, the study rests on the use of established financial indicators (ROE, ROA, ROCE, EBITDA margin, Revenue CAGR, leverage) as valid proxies for firm performance.

Several limitations also deserve mention. The sample size of Search Fund acquisitions remains modest, reflecting the relatively recent diffusion of the model in Europe. Data coverage is not entirely uniform across countries and reporting standards, which inevitably introduces some degree of noise and missing observations. The post-acquisition horizon is limited to three years, meaning that potential long-term effects cannot be fully captured. In addition, the regressions display relatively low explanatory power, a common feature of firm-level analyses where performance is shaped by multiple unobserved factors. Finally, qualitative aspects such as searcher background, governance structures, or cultural integration are not incorporated into the dataset, although they may contribute to explaining outcomes.

These limitations do not undermine the validity of the results but rather frame their scope. Within these constraints, the evidence presented in Chapter 4 remains consistent across specifications and robustness checks, supporting the conclusion that the outperformance of Search Fund acquisitions is primarily attributable to disciplined target selection rather than post-acquisition operational improvement.

Chapter 5 – Discussion and Strategic Implications

This final chapter revisits the central question posed in the introduction—whether the superior performance of Search Fund (SF) acquisitions relative to Private Equity (PE) is primarily the result of post-deal managerial excellence or of disciplined pre-acquisition target selection. It integrates the empirical findings presented in Chapter 4 with the theoretical and practical insights outlined in earlier sections, providing a comprehensive assessment of the research objectives, contributions, and implications. The chapter also outlines the limitations of the analysis and identifies directions for future research.

5.1 Interpretation of Key Findings in Context

The regression results strongly support the central hypothesis advanced in Chapter 3: the superior performance of Search Fund acquisitions is attributable to superior target selection rather than to post-acquisition operational execution. The analyses related to Hypothesis 1 demonstrate that SF-acquired firms display significantly stronger financial performance prior to acquisition than their PE-backed counterparts, with higher ROE, ROA, and ROCE at both $t = -1$ and $t = -2$. This pattern underscores the rigor and discipline characterizing the SF sourcing process.

Conversely, the tests of Hypothesis 2, using both OLS and Difference-in-Differences estimations, reveal no significant evidence of differential post-acquisition improvements between SF- and PE-backed firms. The consistently insignificant interaction terms confirm that the performance gap observed ex ante does not widen after the acquisition.

Taken together, these results validate Hypothesis 3, showing that Search Funds do not outperform because they manage better, but because they buy better. The model should therefore be understood less as a vehicle for radical post-deal transformation and more as an instrument of entrepreneurial arbitrage, where strategic patience and selection discipline drive outcomes. At the same time, it must be emphasized that these conclusions are derived from a relatively small sample of European Search Funds, reflecting the still limited diffusion of the model in this region. As such, the findings should be interpreted with caution and seen as an important but preliminary contribution to understanding the performance dynamics of Search Funds in Europe.

5.2 Theoretical Contributions and Alignment with the Research Design

The empirical strategy of this thesis—combining pre- and post-acquisition comparisons with both cross-sectional and DiD estimators—was specifically designed to disentangle the effects of ex-ante selection from those of ex-post management. By leveraging firm-level financials at $t = -1$ and $t = -2$ to test H1, and Δ performance and DiD regressions to test H2, the study provides a consistent internal triangulation of results.

These findings contribute to the literature by clarifying the conceptual position of the Search Fund model. While often described as a hybrid between entrepreneurship and private equity, the evidence shows that its

value creation dynamics differ substantially from those of PE. Private Equity relies heavily on financial engineering and portfolio diversification, whereas Search Funds derive their strength from selective sourcing and alignment between entrepreneur and target firm. This study thus reinforces the view of SFs as a distinctive form of entrepreneurial acquisition, grounded in filtering and fit rather than in leverage and operational restructuring.

5.3 Practical Implications for the SF Ecosystem in Europe

The results carry several important implications for the European SF ecosystem, which remains relatively young compared to its North American counterpart.

For searchers, the evidence emphasizes that time and effort invested in the sourcing and due diligence phases are decisive determinants of success. Managerial ability matters, but it only creates value when applied to resilient, well-positioned companies. The key is not to "run the business better," but to "buy the right business."

For investors, the findings suggest shifting emphasis from expecting superior post-deal operational improvements to evaluating the searcher's judgment, sourcing strategy, and screening criteria. In practice, this implies supporting searchers in building analytical capabilities, accessing high-quality data, and maintaining discipline in the evaluation process.

For advisors and institutions, the study highlights the importance of training and frameworks that enhance the identification of robust targets. Programmes designed to promote Entrepreneurship through Acquisition (EtA) should prioritize industry analysis, financial screening, and succession dynamics, rather than focusing exclusively on post-deal leadership techniques.

5.4 Limitations and Suggestions for Future Research

While the analysis provides consistent and meaningful evidence, several limitations should be acknowledged.

Sample size: The number of SF-backed firms remains modest, reflecting the still limited diffusion of the model in Europe.

Data quality: Reporting standards vary across countries, especially for privately held SMEs, leading to uneven coverage and some missing observations.

Time horizon: The post-acquisition window is limited to three years, which may not fully capture long-term effects.

Explanatory power: The regressions show relatively low R^2 values, as is common in firm-level studies where multiple unobserved factors influence performance.

Qualitative dimensions: Non-financial outcomes such as employee retention, innovation, or cultural integration are not included, though they may be relevant aspects of value creation.

As for suggestions for future research, several directions appear particularly promising. A first recommendation is to extend the time horizon of analysis beyond five years, in order to evaluate the persistence

of the selection effect and to capture long-run dynamics that are especially relevant in Search Funds, where holding periods are typically longer than in Private Equity. A second recommendation concerns methodological diversification: combining the quantitative framework used in this study with qualitative case studies could offer deeper insight into how searchers actually approach sourcing, screening, and negotiation. It would also be valuable to integrate searcher characteristics—such as professional background, educational attainment, or age—into the empirical design, since these factors are likely to influence both selection strategies and post-deal performance.

Moreover, future research would benefit from replicating this study within the next 24 to 36 months. The European SF ecosystem is expanding rapidly, and in the first half of 2025 the number of acquisitions in Europe surpassed those in the United States, creating a richer and more representative pool of cases. Such an updated dataset would allow for more robust statistical testing and strengthen the external validity of the findings. Finally, an important recommendation is to broaden the set of variables under consideration beyond traditional balance-sheet indicators. Incorporating measures such as customer concentration, industry growth, or recurring revenue patterns—criteria at the core of the SF playbook—would allow future research to assess more precisely whether searchers systematically acquire firms aligned with the theoretical best practices of the model.

5.5 Conclusion

This thesis set out to understand the origins of superior performance in Search Fund acquisitions and to test whether it derives from ex-ante target selection or from ex-post operational improvements. Using a novel dataset of European SMEs and a carefully structured empirical design, the analysis demonstrates that Search Funds acquire stronger companies from the outset and do not deliver significantly greater improvements than Private Equity after acquisition.

From a retrospective perspective, the research has fulfilled the objectives presented in the introduction: to explore the nature of SF outperformance, to apply a rigorous econometric framework to European data, and to provide insights for both academia and practice. The results challenge the conventional narrative that post-deal transformation is the main engine of value creation in entrepreneurial acquisitions. In the SF context, value originates from discipline rather than disruption, from buying well rather than managing better.

The contribution is twofold. Academically, the thesis clarifies the role of target selection as the true driver of SF performance and enriches the literature with one of the first systematic, data-driven comparisons with PE in Europe. Practically, it highlights the importance of searcher judgment, rigorous sourcing, and investor guidance in addressing Europe's succession challenge. Policymakers may also find in the SF model a useful tool for fostering SME continuity and entrepreneurial ownership.

At the same time, the study acknowledges its boundaries in terms of sample size, data scope, and temporal horizon. These limitations, however, open promising avenues for future research, including the analysis of searcher characteristics, the long-run impact of acquisitions, and the incorporation of non-financial outcomes such as customer concentration or industry growth. In light of the rapid expansion of the European SF

ecosystem, this thesis should be regarded not as an endpoint but as a foundation for further exploration and refinement of entrepreneurial acquisition models. Ultimately, the findings highlight a simple yet powerful insight: in the world of Search Funds, selection is not merely the first step—it is the strategy. This conclusion not only clarifies the distinctive value proposition of the Search Fund model, but also provides guidance for investors, entrepreneurs, and policymakers seeking effective solutions to Europe's SME succession challenge.

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