

FOR EXECUTIVES SEEKING TO BUY, SELL, OR RECAPITALIZE BUSINESSES

How To Maximize The Value Of Your Business

Looking At Your Business From An Acquirer's Viewpoint

"Facts do not cease to exist because they are ignored." - Aldous Leonard Huxley

You are contemplating on selling your business and want to understand how best to maximize the value of your business. You might have heard from your industry contacts that some businesses similar to yours sold for 3 times [EBITDA](#) and some others sold for 6 times EBITDA. This variation could mean a difference of several million dollars in take-home! What makes this variation possible? How can you get the best value for your business?

The purpose of this article is to help you look at your business as an acquirer might in valuing your company. The more attractive you can make your business to the acquirer, the better the chance that you will get a higher value for your business. Some key vectors acquirers use in evaluating business are:

1. **Strategic Fit:** Strategic fit occurs when some aspects of your business (products, services, website, distribution channels, location, etc.) are worth a lot more to another player in the industry than it is to you. When a strategic fit is established, the acquirer sees your business on a post acquisition basis and may be willing to offer much more than the going market multiple. Give careful consideration to who the strategic acquirers for your business may be. This is one area where a knowledgeable M&A advisor can be of great help to you.
2. **Cash Flow:** After strategic fit, cash flow is the single largest value driver for most businesses. Think of ways to improve your EBITDA on a sustainable basis. Note that acquirers may be suspicious of short term jumps in cash flow. So, while cutting costs, be careful not to delay hiring or equipment purchases beyond what you believe is reasonable. Once an acquirer starts doubting your credibility, the due diligence increases and the acquirer will make changes to valuation to adjust for the risk.
3. **Management Depth:** Acquirers buy a business that they hope will be functional and growing *after* the sale. It is tough for the acquirer to place a high value on your business if you are the sole decision maker in the company and the business depends largely on your skill set. Developing your staff so that they can run the business when you are gone can pay big dividends when it is time to sell. If you are concerned about your employees leaving once you are gone, it may be good idea to consider employment contracts, stock grants and other incentives that give them a reason to stay long term. If possible, start working on staff related issues at least a year before you plan to start the sales process.
4. **Customer Diversity:** Acquirers are nervous about businesses where a high percentage of business comes from a handful of customers. Ideally, no single customer should contribute to more than 10% of your revenues or profits. The best solution for this

problem is to have long term contracts with your larger customers. If not, you need to diversify the customer base or be prepared to accept earn-outs as part of the transaction price. It may also become necessary to support the acquirer in an advisory role to ensure customer continuity.

5. **Recurring Revenue Stream:** Acquirers love predictable and low risk revenue streams. Any long term contracts, annual service/licensing fees, and other recurring revenue streams make business more desirable and fetch a higher price in the marketplace. In service oriented business, converting predictable customer support calls into recurring revenue stream can turn a business liability into an asset.
6. **Desirable Products & Services That Are Difficult To Copy:** Acquirers place higher value on a business with unique products, services, or distribution systems than a business whose offerings are considered generic. What is unique about your business? Think of ways in which your product/service is unique and why it should be valuable to an acquirer. Having an edge and having the ability to communicate the edge can do wonders to your business's valuation.
7. **Barriers To Entry:** With so much competition all around you, why is your business difficult to copy? Why will the acquirer have as much success with the business as you have had? Is it because of intellectual property (patents, copyrights), regulation (permits, zoning), "difficult to get" contracts (your company is one of the few qualified vendors at each of your major accounts), or something else? Having good answers to these questions indicates that there are barriers to entering your business. These barriers make your businesses more valuable than your competitor's with similar cash flow.
8. **Pending Upsides:** You believe you are about to come up with a compelling new product or make major inroads into a premier customer. You expect these developments will double your business next year and do not want your company to be undervalued based on current financials. Delaying the sale has other consequences that make it unattractive for you to wait. So, what do you do? A good forecast backed up by management presentations with examples on why the company would achieve the forecasts is extremely powerful. However, keep in mind that any forecasts that do not materialize as planned during the sales process can have substantial negative impact on the sales price. Having a good understanding of your product/sales pipeline and having the ability to communicate it with your M&A advisor can help structure a deal where part of the sales price can be paid in earn-out to capture some of the upside.
9. **Industry Exposure:** Perceived industry leadership is an intangible that can enhance your company valuation. Keep a record of newspaper stories, articles in trade magazines, mentions on local TV or any other mention of your company in print or any other media. Your business is more valuable if your company is perceived as being a leader in the industry and is sought after for its expertise. Asking your employees to write articles and keeping in touch with local and industry reporters not only enhances your valuation in the long term but also helps drive your business and image in the community.
10. **Strategic Plan:** A written strategic growth plan that clearly documents the areas the company can grow can be an asset to acquirer. Length of the document is not as important as the content. A well written 2 or 3 page growth plan is sufficient if it conveys the essence of the plan. Prior year plans that show the history of your ventures – along with their failures and successes may also be helpful to acquirers.
11. **Record Keeping:** High quality bookkeeping reduces the risk in a deal and also says a lot about how the business was run. Having a set of clean, easily auditable books inspires confidence and helps during the due diligence and negotiation process.

12. Accentuate The Positive: Every business has its chinks and it is very important for the seller to identify these negatives and proactively offer solutions for turning the negatives into positives. It is important sellers take steps to put out any bad news on the table early on and dealing with issues upfront. Unidentified negatives can haunt you during the negotiating process.

The most important take away from this article should be that while EBITDA matters, EBITDA is not everything. Improvement along the key vectors mentioned above will give you and your M&A advisor a considerable upper hand during the negotiation process. If the EBITDA of your business is \$2 million, the difference between being paid a multiple of 4 and a multiple of 6 is \$4M in pre-tax earnings. Not bad for doing a little bit of homework!

Chak Reddy is a Mergers and Acquisitions Advisor with Elite Mergers & Acquisitions, Inc. [Elite Mergers & Acquisitions](#) specializes in selling businesses with revenues between \$5 million and \$100 million - Businesses too large for business brokers to adequately handle but too small for the national M&A firms. Mr. Reddy is a business M&A and Marketing expert, and is the chief deal maker at Elite. You can reach Mr. Reddy at 916-220-3052 or by email at creddy@elitemanda.com .

For assistance with selling or recapitalizing your mid market company, contact:

Chakradher (Chak) Reddy

Elite Mergers & Acquisitions Inc

creddy@EliteMandA.com www.EliteMandA.com

2260 E. Bidwell St #1114, Folsom, CA 95630

Ph: 800-335-3068; Fax: 888-502-3817

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