

Selling Your Business Ten Steps to Maximize Value

By David M. Kauppi, CBI, President Mid Market Capital

If you are considering selling your business this article will help you evaluate your company as a strategic acquirer might. From that perspective it pays to focus on ten critical areas of value creation. The better your performance in these areas, the greater the selling price of your business. Below is our list of strategic value drivers.

1. Customer Diversity – If too much business is concentrated in too few of your customers, it is a negative in the acquisition market. If none of your customers accounts for more than 5% of total sales, that is a real plus. If you find yourself with a customer concentration issue, start focusing on a program to diversify.

2. Management Depth – An acquirer will look at the quality of the management staff and employees as a major determinant in acquisition price. You should make the move of assigning your successor a year in advance of your scheduled departure date. If you have a strong management team in place, you should try to implement employment contracts, non-competes, and some form of phantom stock or equity participation plan to keep these stars involved through the transition.

3. Contractually Recurring Revenue – All revenue dollars are not created equal. Revenue dollars from a contract for annual maintenance, annual licensing fees, a recurring retainer fee, technology license, etc. are much more powerful value drivers than projected sales revenue, time and materials revenue, or other non-recurring revenue streams.

4. Proprietary Products/Technology – This is the area where the valuation rules do not necessarily apply. If strategic acquirers believe that a new technology can be acquired and integrated with their superior distribution channel, they may value your company on a post acquisition performance basis. The marketplace rewards effective innovation and yawns at “me too” commodity type products or services. Continue to look for ways to innovate in all facets of your business. If you create a technology advantage in your company, think what that could mean to a much larger company.

5. Penetration of Barriers to Entry – In its simplest form, a large restaurant chain buys a small family owned restaurant to acquire a grand fathered liquor license. Owning hard to get permits, zoning, licenses, or regulatory approvals can be worth a great deal to the right buyer. The government market is extremely difficult to penetrate. If your product or service applies and you can break through the barriers, you become a more attractive acquisition candidate.

6. Effective Use of Professionals – Reviewed or audited financials by a reputable CPA firm cast a positive halo on your business while at the same time reduce the buyer’s perception of risk. A good outside attorney reduces the risk even more. A strong professional team is a great asset in growing your business and in helping you obtain maximum value when you exit.

7. Product / Sales Pipeline – Smaller companies often are more agile and have better R&D efficiency than their high overhead big brothers. In technology, time to market is critical and big companies evaluate the build versus buy question. Small companies that develop new technology are faced with the decision of developing distribution internally or selling to a larger company with developed channels. A win/win scenario is to sell out at a price, in cash and stock at closing, that rewards the smaller company for what they have today, plus an earn out component tied to product revenues with the new company.

8. Product Diversity – A smaller company that has a quality portfolio of products but may lack distribution can become a valuable asset in the hands of the strategic buyer. A narrow product set, however, increases risk and drives down value.

9. Industry Expertise and Exposure – Encourage your staff to publish articles and to speak at industry events. Encourage local and industry reporters to use you as the voice of authority for industry issues. Your company is viewed in a more positive light, gets more business referrals, and an industry buyer will remember you favorably as an acquisition candidate.

10. Written Growth Plan – Capture the opportunities available to your company in a two to five page written growth plan. What additional markets could we pursue? What additional products could we deliver to our same customers? What segments of our current market offer the most growth potential? Where are the best margins in our customer base and product set? Can we expand in those areas? Can we repurpose our products for different markets? Can we license our intellectual property? What about strategic alliances or cross marketing agreements? Documenting these opportunities can add to the purchase price.

When it comes to unlocking the market value of your privately held company, it is not limited to the bottom line. Profitability is hugely important, but the factors above can result in significant premiums over traditional valuation approaches. When you sell Microsoft stock, there is no room for interpretation about the market price. The market for privately held businesses is imprecise and illiquid. There is plenty of room for interpretation and the result for the best interpretation by the marketplace is a big pay off when you decide to sell.

David Kauppi is an M&A Advisor with Mid Market Capital, Inc. Dave is a Certified Business Intermediary (CBI), a licensed business broker, and a member of IBBA (International Business Brokers Association) and the MBBI (Midwest Business Brokers and Intermediaries). For more information contact him at (630) 325-0123, email davekauppi@midmarkcap.com or visit www.midmarkcap.com.