

Improving Values and Appeal of Private Businesses

In previous newsletters, we have discussed how industry dynamics and general economic conditions can affect business valuations and exit timing. While business owners should be acutely aware of these external factors, they are typically beyond a company's control. However, owners can control internal factors within the company, and focusing on these internal value drivers can make a real difference in the company's valuation.

It is important to view these drivers from the perspective of potential buyers, and demonstration of strength in these areas not only increases company values but overall appeal, performance, and probability of a successful exit. Based upon our many years of experience assisting companies in positioning for growth and exit, and managing acquisition and sale processes in a broad range of industries, the following fundamental key value drivers surface repeatedly.

Consistent revenue growth and strategy

- Pursuing appropriate growth opportunities such as geographic expansion, new product lines, new customer segments, more effective sales and marketing practices, acquisitions, etc.
- Identifying areas to grow revenue without substantial increases in costs, even if planning to exit the company in the near term. (i.e., utilizing excess capacity in equipment, warehouse space and employees)
- Understanding revenue drivers by analyzing and establishing the means to measure the benefits of investments in advertising and marketing, internal and external sales efforts, social media, etc.
- Companies with diversified customer bases, high customer retention, and multi-year contracts have more predictable repeat sales and are generally able to build revenues faster and more consistently.

Distinct competitive advantages

- Developing unique products, brands and services that provide a competitive differentiation and may include patents, copyrights, and trademarks to protect intellectual property.
- Operating in industries having high barriers to entry for competitors, such as those being capital intensive, requiring licenses, certifications, etc., often allow companies to better control market share.
- Providing products or services having high barriers to exit for customers, such as products and services that are entrenched in the success of those clients, make it more difficult for customers to switch providers.

Strong management team

- Evaluating skills in management required to compete effectively, and building breadth and depth in management teams.
- Making owners less critical to the day-to-day operations of the company by empowering managers with decision-making.
- Providing continuing education and development of employees, including the sharing of strategic goals, to build moral and provide duplication of skills to protect the company against departures of any key talent.
- Establishing financial and other incentives to develop and reward performance and to recognize and retain talent that contributes to improved earnings.

Customer and supplier diversity

- Diversifying the customer base so that the success of the company is not reliant on a few customers. Ideally, no single customer should account for more than 10% of revenue.
- The more diversified the customer base, the higher the perceived value of the business and the lower the risk that the company could materially suffer from a customer loss.
- The same theory applies to suppliers, so as not to rely on just one or two vendors for critical products or services.

Predictable and sustainable earnings, fully supported by quality information

- Building predictable and sustainable earnings by developing strong financial disciplines and information systems.
- Identifying, establishing and monitoring key performance indicators (KPIs) and drivers that are relevant to business decisions.
- Benchmarking company performance and metrics to others in the industry.
- Establishing performance goals and objectives, communicating the objectives to the organization, providing periodic updates as to achievement, and making changes necessary to attain objectives.
- Investing in information systems, including financial and operating systems, to accurately capture and report performance for more effective management, and for supporting to lenders, investors, potential buyers, etc. the consistency and predictability of company performance.
- Developing strong disciplines in budgeting and forecasting to more accurately understand revenue and cost drivers/metrics, and regularly compare forecasts to actual performance to discern variances for making management decisions.

Focusing on the drivers above makes companies more successful and can improve business valuations and probabilities of successful future exits. For certain companies, a well thought out acquisition strategy and process, including a diverse number of targets, can be used to improve or correct issues with many of these value drivers. When a company is ready to exit, running a competitive sale process increases the probability of success and can drive higher values by having multiple competitive bids. Windward Advisors, LLC is experienced in managing formal acquisition and sales processes for our clients. Our next article will focus on one of the most common mistakes owners make in trying to realize value, which can often result in settling for less than optimum value; that of responding to an unsolicited offer and negotiating the “one-off” deal.

Windward Advisors, LLC is a sell-side, buy-side, capital raise, and corporate growth advisory firm. Windward specializes in helping business owners better prepare their businesses, with the intention of increasing shareholder value by providing strategic planning and corporate growth advisory services, and by representing owners in the execution of sales, acquisitions, and financial structuring transactions. Windward is an advocate of ensuring that business owners are knowledgeable about their alternatives and we work closely with other trusted advisors to assist owners with properly preparing before pursuing transactions.

If you are interested in learning more, please contact us for a no cost and no obligation consultation.

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