

EVERGREEN[®] EXITS

UNDERSTAND AND EVALUATE YOUR INDUSTRY TRANSFER STATISTICS



Business owners who are thinking about the future and who will own their business next need to consider one very important question in preparation for a future transition – “Is My Company Transferable to a new owner?” And, moreover, “how do I begin Creating A Transferable Business™?”

In a series of newsletters that we have written, we discussed a number of steps involved with Creating a Transferable Business™. Our next important topic in Creating a Transferable Business™ is an evaluation of Your Industry Transfer Statistics. Having an understanding of how, and for how much money, businesses like yours transfer for in the marketplace is a critical piece of the overall formula for Creating a Transferable Business™. Today’s newsletter takes a closer look at this important topic to further the process of having you think through the transferability of

your business in light of the industry in which you currently exist.

Why Your Industry Matters So Much

Many businesses are successful because the owner’s definition of success includes the profits of the company and what those profits allow the company to do in terms of employing people and providing services to their marketplace while also supporting a personal lifestyle of the owner. However, when you are looking at Creating a Transferable Business™, i.e. one that someone else will want to buy from you and own in the future, you need to consider the activity that exists in your industry and how that activity will either positively or negatively impact your business transfer.

The Buggy Whip Industry

Let's begin with an example. Years ago, many owners of buggy whip companies were able to have their companies run without them because solid management teams were in place. They were profitable businesses and provided solid jobs and lifestyles for the owner and employees. However, as the marketplace changed with technological innovations, i.e. the automobile, the buggy whip industry became one that future investors and owners did not want to invest in. As a result, even the premier buggy whip company saw its transferability diminish, if not disappear completely.

Using this example, you should ask yourself, "is my company a buggy whip provider or a pioneer in the emerging automotive industry?" The answer to this question will begin to guide you in the direction of understanding the level of investment that may be coming into your industry today and helping to support, and possibly provide to you, a future owner for your company.

Multiples of EBITDA, Value for Your Company

Let's assume that the answer to

the question of the future of your industry is not so clear. This is most common because it simply is not all that easy to forecast the future in such a fast-changing world and marketplace. So, let's narrow our inquiry to a conversation around the 'ranges of value' for your business.

Most businesses sell for what is called a multiple of earnings or EBITDA (earnings before interest, taxes, depreciation and amortization). Companies that exist in industries that are in high demand command high multiples of earnings as many interested buyers push pricing higher. By contrast, companies that work within industries that are not as dynamic, i.e. more mature, slower-growth industries, tend to fetch lower multiples of earnings - i.e. lower, overall valuations.

Market Sales as Comparables for Your Exit Value

There are three (3) ways to value a business: the asset approach, the income approach and the market approach. The first measurement - the asset method - is the liquidation value of your hard assets. The next approach - the income method - measures the forecast of future cash flows for your company (and discounts

them back to present-day dollars). The third method is the 'market' method, which is the most intuitive for business owners. This is the method that surveys the price at which similarly-traded companies trade in the marketplace. This market method can help you to initially determine how your industry views your company's viability to attract a buyer - and at what price comparable companies are selling today.

As a caveat to examining private company comparable sale transactions, it is important to note that the data that is available can be hard to read and interpret for its accuracy. While a certain number of data-bases are available to provide certain data, that information is always subject to the interpretation of the people who entered those transactions. In summary, comparable sale transactions are a helpful guide to understanding what buyers are available in the marketplace as well as what level of activity exists in a certain industry. When you know your industry transfer statistics, you are on the path to Creating a Transferable Business™.

Concluding Thoughts

As an exiting owner, it is

important to understand where your company sits in terms of industry activity as well as how many and what type of investors are being attracted to your industry. And, while the day-to-day running of a business requires a myopic focus on management and execution, when you begin to move toward exit planning, we advise that you look deep into your industry in order to manage one of the largest determinates of value for your business, your industry transfer statistics. Once you have a solid understanding of activity and interest within your industry, you can begin to ask better questions about how you might cash in your business one day and begin thinking about how you can grow the business over the next number of years, Creating a Transferable Business™. We hope this newsletter generates some thinking around the valuations within your industry and provides you with a basic framework for applying value in order to assist you with Creating a Transferable Business™.

If you have questions or would like to explore these ideas further, we'd be happy to connect. Reach out to Ed at ed@egwealth.com



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