ATB Entrepreneur's Edge
Transaction Advisory Solutions

ATB Financial

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Plan for tomorrow by enhancing business value today

Regardless of whether the economy is down or up, business buyers continue to search for acquisitions.

Both strategic industry buyers (those looking for synergies with their current companies) and financial buyers (e.g., private equity firms) are active in the Alberta marketplace. In fact, the number of prospective business purchasers, especially financial buyers, has been rising steadily for years.

Globally, between 2000 and 2016, the number of private equity firms tripled, and assets under management more than quadrupled from about $600 billion to nearly $2,500 billion. The North American private equity market is the world's largest, representing more than 57% of the value of worldwide deals in 2015.[1]

How to enhance your company's value

If you're thinking about selling your business, whether soon or in the distant future, this is an important fact to keep in mind. There could be buyers interested in your enterprise.

This then raises the question: is your business in the right shape to appeal to the buyers who would meet your selling goals?

Many Alberta entrepreneurs are experiencing under-performance in their operations as a result of lower oil prices and customer spending. While you may not be intending to sell until this situation improves, your company should be properly positioned for a sale when the timing is right. This requires optimizing value in areas of your operation that will appeal to buyers' expectations.

In this issue of Entrepreneur's Edge, we outline what purchasers are looking for and how you, as a business owner, can enhance your company's value to increase sales potential and selling price.

[1] Private Equity Outlook 2017, Toptal

Ten ways to build measurable value

The following ten suggestions help drive business value. Entrepreneurs who can execute them will experience benefits not only when they're selling a business, but also when they're securing financing or planning their retirement or estate.

1. Prepare Early

Early preparation will ensure a sale that delivers optimal value for the business you have invested years or decades building.

Properly positioning a company can sometimes take years of advance preparation. As well, the sales transaction process may take several months to complete. The Pepperdine Private Capital Markets Project found that 82% of business transactions require five to 12 months to close while 14% take more than one year.[2] It's also important to keep in mind that many buyers expect post-closing transition commitments from owners that can range from one to five years.

So, if your plan is to retire within the next few years, you should start preparing your business for sale now.

2. Create an action plan

Similar to preparing a house for sale, a business needs an action plan to achieve the target sales price.

Professional advice can be particularly helpful in preparing this plan. Experienced transaction professionals can objectively evaluate the strengths and weaknesses of your operation and the specific steps required for your business to fetch the best possible price and terms.

They will generally start by assessing the current value of your enterprise (refer to Entrepreneur's Edge, Valuing your Business). This assessment yields insights into the quality of your operation, EBIDTA margins, debt, cash flow, profitability, growth expectations and risk. By having this assessment completed by an independent third party, you'll gain a better understanding of how these factors impact the overall value of the enterprise from the perspective of potential buyers.

Documenting the findings and recommendations and establishing timelines transforms this information into a practical action plan. Your management team can regularly review this to monitor progress and continue building value.building value.

[2] 2017 Private Capital Markets Report, Pepperdine School of Business and Management

3. Estalish a sustainable management team

Buyers want assurance that a business can thrive in the absence of the owner. If your company is heavily dependent on the owner's skills and relationships with customers and suppliers, it won't be attractive to buyers.

Most purchasers want to see a team in place that can lead the business after the transfer of ownership.

If you have a second-in-command or other talented managers, it's important to mentor them to lead the business. Without a reliable team in place, a financial buyer will likely ask for the owner's full commitment for three or more years post-sale in order to allow sufficient time to develop such a team.

Buyers also like to be assured that key employees will stay on; therefore, having employment agreements with key personnel increases corporate value.

4. Clean up debt

To a potential purchaser, most of the value of a business lies in its ability to generate positive cash flow. Buyers calculate debt into amounts they offer sellers.

If your business has a high debt capacity, this enables a buyer to borrow more cash against the company, which means they are likely to pay a higher price for it.

Prospective buyers will assess whether an owner is using debt astutely to support growth and expansion or whether the company is so highly leveraged that cash flow or profitability are negatively impacted.

For future sellers, reviewing the capital structure and debt capacity of the operation and, if necessary, reducing detrimental debt, can generate excellent future returns.

5. Trim fat from the balance sheet

Privately held businesses often hold personal assets that contribute little to operations. Items such as an owner vehicle, vacation home, boat, snowmobile, art and so forth clutter balance sheets and look messy to potential buyers.

Review the balance sheet for opportunities to eliminate items like these, along with equipment or other fixed assets, that are no longer in use and won't add value to a sales transaction.

Also review off-balance sheet liabilities and contingencies for opportunities to enhance value. Items like purchase commitments, incentive plans and pending litigation and environmental liabilities should be addressed to minimize negative impact.

6. Separate the personal from the business on the income statement

Most owners deduct some personal expenses through the business such as vacations, family member compensation, golf memberships, life insurance, personal vehicle expenses and mobile phones. Since these expenses are unnecessary for operating the company, purchasers will make "normalizing adjustments" to the seller's income statements when valuing a potential acquisition. This removes personal expenses, making it easier to determine the company's actual operating performance and financial position.

You can help clarify the returns from normal operations for prospective buyers. By removing personal expenses where possible or by clearly documenting them so they are readily identified when assessing business value, you can effectively normalize the income statement to increase value.

7. Optimize the capital expenditure investments

Owners spend money on capital expenditures (capex) to either grow or maintain their business. When assessing a potential acquisition, buyers calculate free cash flows by determining the amount and purposes of the capex, as well as whether it is internally financed or relies on debt.

Buyers want to know if they have to use their own capital to fund growth; how much internal cash is spent on capex, since this detracts from funds available for debt payment; or whether the company is spending so little on capex that they would have to invest significantly in the business to achieve their goals. What they find could substantially influence the purchase price they offer.

Entrepreneurs with capital expenditures should track the amounts used to grow and maintain the operation and the amounts that are financed with company cash and bank debt. Transaction professionals can provide recommendations for the optimal capex balance to appeal to potential buyers.

8. Strengthen financial controls

Comprehensive financial controls not only safeguard company assets, they also demonstrate effective business management to prospective purchasers.

Buyers like to see an experienced controller or chief financial officer in place as assurance that financial controls are reliable, financial statements are accurate, reporting is timely and someone is tracking key performance indicators.

They also like to see audited financial statements for at least three to five years prior to a sale. Having a qualified individual overseeing financial statements and controls during this period of time provides reassurance to potential purchasers on multiple levels.

9. Update customer and supplier agreements

Customer and supplier contracts translate to sustainable cash flow and revenue streams to purchasers.

Buyers like recurring revenue models that limit the risk of customer terminations impairing the business.

Having up-to-date contractual agreements provides reassurance that customers and suppliers will continue working with your company after the transfer of ownership.

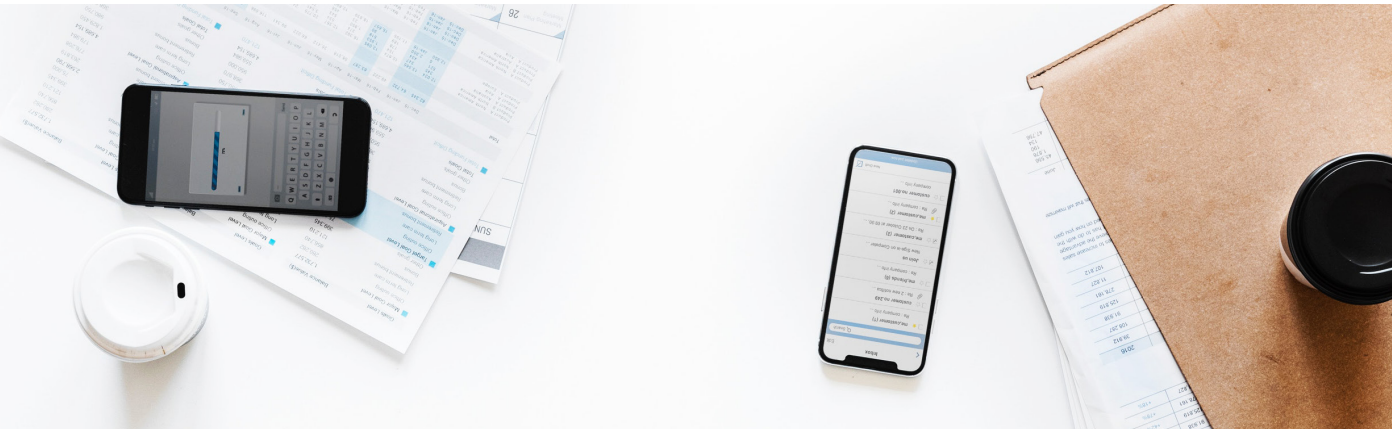
Buyers also like to see diversified customer and supplier bases. If any single customer accounts for more than 10% of revenue, you should consider diversification options.

10. Communicate a clear vision and culture

Buyers are focused on the future, or, the potential of an acquisition. A seller can therefore attract buyer interest by painting a compelling vision of its opportunities for growth.

A powerful vision also helps to communicate the company culture. Prospective purchasers want to know that the culture of an organization is strong and cohesive, employee morale is high and turnover is not a problem.

Clearly articulating the vision and goals for your business and employees helps buyers visualize what is possible.



Be ready

Unexpected events—an illness, an accident or even an unsolicited offer for your business—could happen at any time. Be ready.

Structuring the sale of your business involves integrated financial, tax and legal issues. Connect with experienced M&A, legal, accounting and tax advisors who are experienced with corporate transactions for privately held businesses. They can provide objective perspectives and expert guidance to smooth the transaction process and expedite a deal.

With the right action plan and advisory team, you can preserve the value of your business and be confident that it will generate the returns you deserve for your years of hard work.

Let's have a conversation.

It's never too early to discuss the potential sale of your business.

Even if a transaction may be years away, the ATB M&A team would be pleased to meet with you to discuss opportunities for adding value to your enterprise to position it for a future sale.

We help entrepreneurs who have businesses with an enterprise value of $5 million-plus achieve the best sale price, deal structure and timing. Our support extends beyond value assessments to include prospective-buyer identification, sale-document preparation, knowledgeable transaction advice, facilitation of communication among the parties and assistance with negotiations and timely deal closing.

Contact an M&A Advisory Services team member today to begin a confidential conversation about positioning your business for a rewarding future.

About Entrepreneur's Edge

For more information on this or past reports, or to subscribe to our mailing list, visit ATB.com/EDGE

ATB Financial M&A Advisory Services

The ATB team of mergers and acquisitions specialists is focused on helping Alberta entrepreneurs identify opportunities and resolve challenges related to growth, transition and transactions through every stage of the business life cycle.

About Entrepreneur's Edge

This quarterly publication is intended to provide Alberta entrepreneurs with timely information and insights to realize successful business transactions.

Our team offers deep knowledge of the marketplace, exceptional sector expertise and resources of our bank's industry specialists, and a strong North American network of professionals, buyers, sellers and investors.

Growth	Transition	Transactions
Recapitalizations	Succession planning	Business sale mandates
Mergers and acquisitions	Employee share ownership plans	Management buy outs

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