Cash today, wealth tomorrow: Building the value of your business for sale

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Introduction

Getting the most out of your business

At some point, and it may be many years in the future, your ownership of your business will come to an end. Whether it's a planned or unplanned exit, your role as owner-manager will reach a conclusion. It's one of the few certainties in running a business.

At any stage in your company's evolution, you're making two precious investments: your money and your time. One day in the future, you'll no doubt want a return on that investment. You'll want to take out of the business money to build your personal wealth and increase your security, and time to spend on other important things in your life (whether that means retirement, an exciting new business venture or another long-held ambition).

'The work you do now to boost the value of your business will ensure you get maximum value in the future.'

The things you focus on today will have a direct bearing on how successful that conclusion will be – namely, how attractive and valuable your business will be to potential buyers. The work you do now to boost the value of your business will ensure you get maximum value in the future. And, as a bonus, in the meantime, you'll be owning a more profitable, successful business that's easier to run.

This guide helps you understand the value of your business and identify key value-boosting activities that will set you and your business in good stead for whatever future you may choose. >

What if you're nowhere near ready to sell?

That's fine. You don't need to be actively looking to sell to start thinking about the value of your company. Boosting your business's value is part of good exit planning – and exit planning is an important consideration at any stage of a business because it gives you greater control over your future.

Your objectives for owning and running a business will vary and what you want now may be very different to what you want in the future. Today, your focus may be on improving cash flow, winning new clients or maybe enjoying yourself by running a business that's fulfilling. In the future, whether that's next year or two decades from now, your focus may change.

The point of exit planning and building the value of your business is to help prepare you for any scenarios or a change in circumstances or priorities in the future.

7 benefits of exit planning and boosting the value of your business

1. **You'll have a better-run business that's less dependent on you, the owner.**
2. **Should an unexpected approach be made to buy the business, you'll be better positioned to deal with it.**
3. **You'll be in a stronger negotiating position in any business partnership discussions.**
4. **Your business will be more attractive to an investor.**
5. **You'll be better positioned to raise money with a loan.**
6. **The business will be more resilient, with stronger management and controls.**
7. **You'll be in the best position to extract maximum value for you and your loved ones in the future.**

Understanding the value of your business

Many owners ask the question, ‘how much is my business worth?’ and some ask, ‘how much could my business be worth?’ Both are good questions and neither has a definitive answer that means much until someone commits to buying the company from you at a price you’re willing to sell at.

Accountants, business valuation experts and business advisers will usually come up with a figure based on the current financial state of your company. The valuation may be calculated based on the net assets in the business or using an industry standard multiple such as ‘5 x EDITDA’ (EBITDA is a measure of profit that excludes the effects of interest, tax, depreciation and amortisation). Taking a nice round number as an example, if a business is achieving an EBITDA of £1m, it could potentially be sold for five times that: £5m.

Profit is the obvious measure sought by a potential buyer, so it is in your interests to identify ways to improve that figure. For example, finding cost savings to bring EBITDA to £1.1m would increase the potential value of the business to £5.5m.

Just as important, however, is the ‘multiplier’ – 7 x EDITDA is a lot more potential wealth for the selling owner than 5 x EDBITDA. And that multiplier can be influenced by lots of different factors. For example, if there are six potential buyers looking at the business, this level of interest could enhance the multiplier. This is because, for certain buyers, the prospects of the company, when combined with their own business, become more important than the current financial performance. Some of the factors affecting the multiplier are a lot less tangible than others and we look at some examples later in the paper.

‘Valuation methods are, at best, a starting point.’

This is the danger with business valuations. In our experience, valuation methods are, at best, a starting point and, at worst, a distraction when it comes to building the value of your business. What you will ultimately get for your business is what someone is prepared to pay and even then, that figure may be based on certain conditions or phased payments.

All this means that, as well as doing all you can to increase the profit side of the equation, you also need to work hard to make your business as attractive as possible to potential future buyers.

What makes a business attractive to buyers? (Hint: it's not all about profit)

Financial results alone are not the only determinant of how attractive a business might be, nor are they a reliable guide to the amount a potential buyer might be prepared to pay. The value of a business can be influenced by many factors.

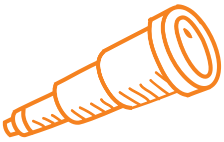
> 'There's nothing that a buyer wants more than a well-run business with excellent prospects.'

Essentially, there's nothing that a buyer wants more than a well-run business with excellent prospects. Therefore, to achieve maximum value, your business needs to be an all-round great package. As a bonus, we bet a well-run business with excellent future prospects is exactly the kind of business you want to run for yourself in the meantime. By developing your business as if you're aiming to attract a potential buyer, you end up with a more efficient and profitable company that's easier to run.

One of the biggest issues, and the reason it's the first question in our questionnaire (overleaf), is the dependency of the business on the owner. If key activities, relationships and knowledge lay only with the owner, it won't matter how much profit the company is making, it'll usually be less attractive to a buyer – even if you are willing to stay on in the business – and therefore worth less. By the same token, this dependency and time commitment also inhibit other business growth strategies for the company and personal aspirations of the owner. If you are your business, and it simply cannot function without you, this is something that needs addressing.

5 scenarios where you'll be glad you thought about exit planning

1. **You want to make a partial exit from the day-to-day running of the business, without selling up.**
2. **A potential buyer makes an unexpected offer for your business. How well prepared are you to handle the approach and secure the best outcome?**
3. **You want to start a new venture, and may need to release all or some of your time and money to invest in the new enterprise.**
4. **You're forced to take time away from the business due to illness or other circumstances. Putting in place a strong management team allows you to take a step back while retaining your ownership.**
5. **A new market or opportunity arises and you want to sell part of the company to raise the necessary finance.**



Is my business attractive to buyers?

To assess the attractiveness of your company, ask yourself the following questions. If the answer to any of these questions is no, then this indicates priority areas for improvement. Head to the section entitled 'How to increase the value and attractiveness of your business' for advice on addressing these issues.

	Yes	No
1. Can the business function independently of me, the owner?		
2. Do I have a good management team in place?		
3. Does our income come from contracted/recurring revenues?		
4. Do we have tied-in suppliers?		
5. Is our employment record squeaky clean?		
6. Do we have a strong brand and reputation?		
7. Do we have a diverse range of clients?		
8. Do we have new products or services in the pipeline?		
9. Have we protected vital assets like intellectual property?		
10. Do we have relevant and accurate management reporting?		

Case Study

Increasing value in a chartered accountancy firm

Henchards worked with one accountancy firm to boost its value and, ultimately, make it more attractive to buyers. Having evaluated the business and identified various areas for improvement, our work focused on three core strands:

1. Looking at organic growth and acquisition opportunities to increase scale and operating profit. This strategy centred on great service, value-based pricing and strong relationship development. As a result, significant growth was achieved through existing clients and referrals. In addition, two local businesses were acquired, further boosting growth. In the period of working with Henchards, the company's fee income grew by over 70%.
2. Concentrating internal resources on client services and outsourcing activities such as HR, marketing and IT support to reduce costs. This, in turn, helped improve operating profit.
3. Developing the brand to become the most dynamic and recognised brand in the local business market. This was delivered as a programme of marketing events and charitable activities, all effectively promoted through both PR and social media.

After a few years of working with Henchards, the business successfully became part of a national and international audit, tax and consulting firm, thus completing the exit plan and releasing wealth and time for the directors to move on to new projects, both professional and personal.

How to increase the value and attractiveness of your business

There are many practical things you can do to make your business more valuable and attractive to buyers, and our top 10 value-boosting activities below tie in with our earlier questionnaire. If you answered 'no' to any of the questions we asked, you'll want to address those items as a priority.

Step 1: Make sure the business isn't dependent on you

If the business is dependent on you for its everyday functions, this will seriously put off potential buyers and impact the value of your business. There are lots of things you can start doing now to reduce your business's dependency on you. These include creating a contingency plan for when you're not around, taking breaks away from the business to see how well your team cope, introducing clients to key personnel within the business (as opposed to holding all the client relationships yourself), and delegating or outsourcing everyday tasks, such as billing.

Step 2: Create a strong management team

Building a strong management team and learning to delegate is a crucial step in building value – as well as making your business easier and more pleasurable to run. It's therefore worth bringing people into the company in management positions, or supporting those in your team to take on greater responsibility.

Step 3: Maximise repeating revenues

Prospective buyers are risk averse when it comes to future revenues, and your past sales performance does not guarantee the same going forward. Repeatable revenues and subscription services, greatly 'de-risk' future revenues. A major trend in markets as diverse as software and shaving products is the 'subscription model'. Rather than offering products to customers as one-off purchases, you might look at building a service that charges a monthly fee for online software access or for delivery of a month's supply of shaving products, for example.

Step 4: Lock in your suppliers

Buyers like to know exactly what they're getting into, and a business with firm, tied-in suppliers working to set contractual terms and prices is a much more attractive prospect than a business that's winging it. Therefore, wherever possible, tie in your suppliers and get firm commitments that reduce uncertainty for the future.

Step 5: Smarten up your employer brand

Iffy employment practices will undoubtedly dent your company's reputation and, in turn, affect its value and attractiveness to potential buyers. If your company has had issues with employee contracts, salaries, hours, working conditions or employee engagement, you need to demonstrate that you're taking real steps to remedy these. >

Step 6: Enhance your company brand and reputation

There's no doubt that having a strong brand and reputation makes your business more valuable. If you think about the world's most successful brands like Coca Cola, Disney or Apple, their brand makes them far more valuable than the combination of their physical assets and intellectual property. You may need to invest in specialist branding help, but it's an investment that will add value to your business.

Step 7: Build up a diverse range of clients

Having a high proportion of your revenue from a single client or similar group of clients leaves you vulnerable and reduces the attractiveness of your business. Therefore, you must be able to demonstrate that your client base is diverse and robust. Look at your sales and marketing activities and your proposition to see how they can be flexed to attract new types of clients or enter new markets.

Step 8: Look to the future with new products and services

Buyers want a business with its best years ahead of it, not behind it. This means they'll want to see a clear direction and pathway to future growth with new products or services. You've probably already got a growth strategy in place; is it still fit for purpose? If not, a business adviser will be able to review your strategy and root out opportunities for new products and services.

Step 9: Protect your intellectual property

IP is often overlooked as a business asset, yet it can be one of the most valuable assets your business has. Anything unique that your business physically creates is IP, including your brand, product designs and the products themselves. You can protect valuable IP by trademarking your brand or product name, patenting inventions and registering designs with the Intellectual Property Office.

Step 10: Have good measurement, controls and reporting in place

This is a powerful way to demonstrate great management and provide compelling evidence of success. Having good measurement, controls and reporting certainly helps when responding to a buyer doing their due diligence, but it also enables you to attract potential buyers and enhance the multiple on your business. Instead of simply relying on your standard accounts reports (and do you even have these?), look to analyse key ratios such as the cost per lead, revenue per employee and how many times your revenue covers your overheads.

Finally, keep in mind the importance of finding the right buyer for your business. You can take all the right steps and make all the correct decisions on building the value of your business, but, as we said earlier, the value you get is the price someone is willing to pay. And the interesting point is that, for the same business with the same financial record, different buyers will pay a different price. When you start to consider a sale, think carefully and seek help in identifying potential buyers who would value your business sufficiently to pay a premium. These 'strategic' buyers can make a huge difference to the wealth you generate from the sale of your business.

Conclusion

Cash today, wealth tomorrow

Managed well, your business should give you cash today and wealth when you sell, whenever that may be.

The beauty of building the value of your business now is that it puts you in a position where you have a choice of continuing to run a successful, attractive business yourself or selling the business at a time that's right for you and your family. For us, it's not about having one eye on the 'exit' sign – it's about creating greater flexibility and making room for exciting new opportunities in the future, whether business or personal.

Working with a business adviser is a great way to boost the value of your business. To find out how Henchards can help you plan for the future while building the kind of company you want to run today, contact us on **01276 858199** or email us at **enquiries@henchards.com.**